

70 FR 9041, February 24, 2005

A-821-819
Investigation
Public Document
IA I (6): JGR

February 16, 2005

MEMORANDUM TO: Joseph A. Spetrini
Acting Assistant Secretary
for Import Administration

FROM: Barbara E. Tillman
Acting Deputy Assistant Secretary
for Import Administration

SUBJECT: Magnesium Metal from the Russian Federation: Final Determination of
Sales at Less-than-Fair Value
Issues and Decision Memorandum

I. Summary

We have analyzed the comments in the case and rebuttal briefs submitted by interested parties in the antidumping duty investigation of magnesium metal from the Russian Federation. As a result of our analysis, we have made the appropriate changes in the margin calculation. We recommend that you approve the positions we have developed in the Discussion of Interested Party Comments section of this memorandum.

II. Background

On October 4, 2004, the Department of Commerce (the Department) issued its preliminary determination in the antidumping duty investigation of magnesium metal from the Russian Federation (Russia). See Notice of Preliminary Determination of Sales at Less Than Fair Value and Postponement of Final Determination: Magnesium Metal From the Russian Federation, 69 FR 59197 (Oct. 4, 2004) (Preliminary Determination). The period of investigation (POI) is January 1, 2003, through December 31, 2003. We invited parties to comment on the Preliminary Determination. On January 7, 2005, we received case briefs from the Petitioners,¹ Northwest Alloys, Inc. and Alcoa, Inc. (collectively, Alcoa),

¹ The Petitioners in this case are, collectively, U.S. Magnesium LLC (U.S. Magnesium), United Steelworkers of America, Local 8319, and Glass, Molders, Pottery, Plastics and Allied Workers International, Local 374.

and both Respondents.² On January 12, 2005, we received rebuttal briefs from the Petitioners and both Respondents.

III. List of issues

General Issues

1. Scope of the Order - One or Two Classes or Kinds of Merchandise
2. Electricity Costs - Whether to Disregard or Adjust Reported Electricity Costs to Account for Distortions in the Russian Electricity Sector
3. Barter Sales

Company-Specific Issues

A. Avisma

4. Sales Through Bonded Warehouse
5. Model Matching of Certain Avisma Products
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7. Payment Dates for Certain Home-Market Sales
8. By-Product Credit
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13. Model Matching of Certain SMW Products
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² The Respondents in this case are JSC Avisma Magnesium-Titanium Works and VSMPO-Tirus, U.S. (Avisma), and Solikamsk Magnesium Works (SMW).

24. General and Administrative Expenses - Solikamsk Desulphurizer Works (SZD)

IV. Discussion of Interested Party Comments

Comment 1: Scope of the Order - One or Two Classes or Kinds of Merchandise

Both Avisma and Alcoa argue that the Department erroneously determined that pure and alloy magnesium constitute one like product. They claim that the Department should find that pure and alloy magnesium constitute separate classes or kinds of merchandise. Avisma and Alcoa point out that the International Trade Commission (ITC) found two like products in its investigation of this case and that historically the Department has also found pure and alloy magnesium to be separate classes or kinds of merchandise. For example, Alcoa notes that in Pure and Alloy Magnesium from Canada and Norway (1992), Pure and Alloy Magnesium from the People's Republic of China, the Russian Federation, and Ukraine (1994), and Pure Magnesium from China, Israel, and Russia (2001), the Department found separate classes or kinds of merchandise. In the instant case, Alcoa claims that the Department has not provided any basis for its departure from past precedent.

Alcoa states that, in its Preliminary Determination, the Department uncritically accepted the Petitioners' arguments. According to Alcoa, one of the basic flaws in the Petitioners' submissions flows from a misunderstanding of the nature of beryllium. Alcoa and Avisma state that most alloy magnesium products contain beryllium, a known carcinogen, and therefore cannot be used in the production of aluminum beverage cans. Further, Alcoa claims that while the Petitioners noted a minute trace tolerance for beryllium in Alcoa's sourcing specifications, beryllium occurs naturally and is impossible to remove entirely. Alcoa's references to "beryllium-free" magnesium refer to magnesium to which beryllium has not been intentionally added. Alcoa concludes that the amount of beryllium that Alcoa deems acceptable is less than the amount of beryllium typically required in alloy magnesium applications.

Avisma and Alcoa state that in evaluating whether products should be classified as separate classes or kinds of merchandise, the Department determines whether there is a clear dividing line between product groups. Avisma and Alcoa claim that there is a clear dividing line between pure and alloy magnesium based on the five criteria in a Diversified Products analysis. See Diversified Products Corporation v. United States, 572 F. Supp. 883 (1983) (Diversified Products). First, they have different physical characteristics and are classified under separate Harmonized Tariff Schedule (HTSUS) subheadings.

Second, the ultimate purchasers have different expectations as to form, quality, and purity. Third, they have different ultimate uses: pure magnesium is primarily used in alloying aluminum, as a chemical reagent in steel desulphurization, and as a reducing agent for various nonferrous metals, while alloy magnesium is primarily used in die-casting. In certain applications, alloy magnesium can be used as a substitute for pure magnesium; however, such substitution is limited to alloy products that are beryllium-free. In contrast, beryllium is a requirement in die-casting applications. Fourth, they have different channels of trade: pure magnesium is sold to aluminum producers and to steel manufacturers; alloy magnesium is primarily sold to die-casters (there is only a limited channel of distribution where some types of alloy are sold to certain aluminum producers and steel manufacturers). Finally, the focus of marketers in advertising the respective qualities of these two products differs significantly due to the two distinctive end-use markets. Alcoa notes that there is no evidence on the record with regard to marketing that suggests the Department should depart from its past precedent.

Alcoa strenuously objects to the Department's "embrace" in the Preliminary Determination of certain statements made by the Petitioners to the effect that beverage-can-stock producers are willing to use alloy magnesium with beryllium content, or have the technology to render the beryllium content innocuous either through special coatings on the beverage-can walls or through diluting the beryllium-containing alloy by mixing it with pure magnesium. Alcoa states that: 1) it is concerned with its workers processing alloys containing beryllium, not just with consumers ingesting beryllium, and diluting beryllium content might protect the consumer but not the worker; and, 2) at least some of the Petitioners' assertions are hypothetical. Alcoa stresses in unequivocal terms that it "does not use any magnesium alloy containing any intentional additions of beryllium." It also states, however, that it uses alloy magnesium containing naturally occurring amounts of beryllium not in excess of 1 part per million, which it refers to as "beryllium-free" magnesium. Of the latter type, it states that it has used only a "very limited amount."

According to the Petitioners, the Department cited new information which was not on the record of its previous determinations, showing that alloy magnesium is used as a substitute for pure magnesium. The Petitioners note that the Department's previous finding of two classes or kinds of merchandise was 13 years ago and that technology has advanced to the point that two-way substitution is now possible. Further, the Petitioners argue that applying the Diversified Products criteria clearly indicates one class or kind of merchandise.

Department's Position:

In our Preliminary Determination, we conducted our analysis of the scope of this investigation based on the five criteria of Diversified Products and concluded that pure and alloy magnesium constitute one class or kind of merchandise. See Memorandum to Barbara Tillman, Magnesium Metal from the Russian Federation: Like Product and Scope Issues, Sept. 24, 2004 (Product Memo) A public version of this memorandum is available in the Central Records Unit, Room B-099 of the Main Commerce Building (CRU). Specifically, we found that:

- pure and alloy magnesium share similar product characteristics, namely that they are lightweight, low-density metals with a high strength-to-weight ratio.
- the expectations of the end users are generally the same: ultimate purchasers of most varieties use magnesium for its primary product characteristic, namely that of a high strength-to-weight ratio.
- in certain sectors of the magnesium industry pure and alloy magnesium are used interchangeably.
- the channels of trade are not different for pure and alloy magnesium: sales are made mainly to end users and the same sales representatives generally market both products.
- there was no evidence on the record of any differences in the manner in which the two products were marketed and advertised.

After reviewing our analysis in light of the comments of the parties, we determine again, as we did in the Preliminary Determination, that the scope of this investigation includes only one class or kind of merchandise.

It is apparent from the parties' arguments that one issue underlies the application of all five Diversified Products criteria: whether pure and alloy magnesium are interchangeable, or more specifically, whether alloy magnesium is an acceptable substitute for pure magnesium. Nearly every argument made under each of the five criteria comes back to this same question.

We do not think it is necessary, however, to resolve the dispute between the Petitioners and Alcoa over whether the alloys Alcoa uses contain "intentionally added" beryllium, or whether Alcoa theoretically could use such alloys through coating beverage-can walls or diluting these alloys with pure magnesium.³ There is ample evidence on the record, including statements by Alcan, Alcoa, and Halaco, a U.S. producer of secondary alloy magnesium, to conclude that alloy magnesium, with and without beryllium, can be used as a substitute for pure magnesium in certain applications of the aluminum industry and the iron and steel desulfurization industry. This evidence and its relevance to the five Diversified Products criteria is discussed in detail in the Product Memo, and our analysis for the final determination adopts the reasoning stated therein. While there may not be complete substitutability, a finding that two different types of a product constitute one class or kind of merchandise does not require a determination that one product is an identical replacement for the other, but only that one product can be used as a substitute for the other. See, e.g., Wirth, Ltd. v. United States, 5 F. Supp. 2d 968, 980 (CIT 1998).

³ However, we agree with the Petitioners about Alcoa's vagueness in some of its assertions. Alcoa never stated in a timely manner, for example, what the grade is of the "beryllium-free" alloy magnesium it uses, how much it uses, or how it uses it. It is difficult to evaluate Alcoa's arguments without knowing the answers to these questions. (Alcoa did finally state the grade of the product during the public hearing. However, the information provided at that time was clearly untimely submitted and could not be taken into account by the Department in reaching its final determination.)

With respect to Avisma's and Alcoa's argument that the Department does not distinguish this determination from apparently contradictory determinations in prior investigations of magnesium, we note that in every case, the Department must make a determination using the facts on the record of that proceeding. We can only speculate about why certain facts on the record of this investigation were not on the record of prior investigations concluded in 1992, 1995, and 2002. It may be that both technological or economic changes in the magnesium and/or aluminum industry have allowed or encouraged the substitution of alloy magnesium for pure magnesium products that was not possible in the past. In this regard, we note the following excerpt from the ITC transcript in its concurrent investigation, recording testimony by an official of the aluminum producer Alcan, traditionally a user of pure magnesium, but now a user in part of recycled (*i.e.*, alloy) magnesium:⁴

The biggest change in the magnesium industry is . . . the development of new technology that permits the domestic production of high-quality magnesium from scrap material. This change has had the most dramatic impact on Alcan's decisions regarding the sourcing of magnesium.

In 2002, this technology was essentially non-existent. By 2003, Alcan was sourcing a significant proportion of its magnesium from a domestic source and has the capability of recycling magnesium scrap in the secondary magnesium. We forecast that there will be a proportion of our magnesium needs that will be fulfilled by recycled materials that will continue to grow dramatically over the next few years as more sources are qualified and will surpass the quantity of magnesium source from other domestic and foreign sources.

ITC Conference Transcript: Magnesium From China and Russia, Investigation Nos.: 731-TA-1071 and 1072 (Preliminary) at 118 (emphasis added).

In reading the above excerpt it is important to note that no parties to this investigation contest the fact that recycled magnesium is recycled alloy magnesium, and that recycled alloy magnesium is likely to contain beryllium since die casters constitute the largest consumer group of alloy magnesium, another fact on which parties appear to agree. Thus, according to this statement, 2003, the year after the conclusion of the previous magnesium investigation, was a watershed year for the magnesium and aluminum industries, allowing for greater use of alloy magnesium where only pure magnesium had been used before.

Comment 2: Electricity Costs - Whether to Disregard or Adjust Reported Electricity Costs to Account for Distortions in the Russian Electricity Sector

⁴ We referred to this page of the transcript specifically in a letter to parties on June 9, 2004, and requested that parties provide us with comments on this testimony.

The Petitioners argue that the Department has the legal authority to adjust the Respondents' reported energy costs to account for recognized distortions in Russia's energy sector. In the Petitioners's view, section 773(f)(1)(A) of the Tariff Act of 1930, as amended (the Act), which states:

Costs shall normally be calculated based on the records of the exporter or producer of the merchandise, if such records are kept in accordance with the generally accepted accounting principles of the exporting country (or producing country, where appropriate) and reasonably reflect the costs associated with the production and sale of the merchandise.

affords the Department discretion to adjust the Respondents' reported costs. The Petitioners note that the use of the word "normally" is evidence that, although there is a preference for the use of information recorded in an exporter's or producer's records, the Department still has the authority to use other information when those records do not "reasonably reflect the costs associated with the production and sale of the merchandise." The Petitioners claim that because energy costs are a significant input into the cost of production of magnesium, and because these costs are distorted, as demonstrated by the information in the record, the Department, according to the language above, has the authority to turn to other information when calculating the energy costs in this case.

The Petitioners claim that their interpretation of the statute is fully consistent with the obligations imposed by Article 2.2.1.1 of the World Trade Organization (WTO) Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade of 1994 (ADA), which uses language very similar to section 773(f)(1)(A) of the Act. In the Petitioners' view, production costs that are kept in accordance with Generally Accepted Accounting Principles (GAAP) but fail to reflect the costs associated with the production and sale of the product under investigation, are not acceptable under Article 2.2.1.1. The Petitioners further note that at least one WTO Panel has affirmed this interpretation. In addition, the Petitioners argue that the European Commission (EC) has relied on the same ADA provision in administering its antidumping law and cite two cases in which the EC disregarded the reported energy costs based on the finding that Russian energy prices do not reasonably reflect the costs associated with the production of electricity.

According to the Petitioners, the Department has already recognized its statutory authority to adjust for Russian energy cost distortions when calculating dumping margins in a recent suspension agreement (see Suspension of Antidumping Duty Investigation of Certain Cut-to-Length Carbon Steel Plate from the Russian Federation, 68 FR 3859, 3861, n.3 (January 27, 2003) (Cut-to-Length Steel Plate from Russia)). Similarly, according to the Petitioners, in the Memorandum from Albert Hsu, Senior Analyst, et. al., to Faryar Shirzad, Assistant Secretary, concerning the Inquiry Into the Status of the Russian Federation as a Non-Market-Economy Country Under the U.S. Antidumping Law, (June 6, 2002) (Graduation Memorandum), the Department has clearly stated that it has the authority to disregard certain prices and costs, and in particular energy costs, when "the costs do not reasonably reflect the costs associated with the production and sale of subject merchandise."

In the Petitioners' view, the Department's exercise of its statutory authority in this case is crucial for

ensuring that the dumping margins are calculated as accurately as possible, as required by the statute. In support of their argument, the Petitioners point to the Department's longstanding practice, in adherence with this statutory mandate, to disregard or adjust reported costs, even when GAAP-conforming, when those costs do not reasonably reflect the costs associated with the production and sale of the subject merchandise (see, for instance, Notice of Final Determination of Sales at Less Than Fair Value: Carbon and Certain Alloy Steel Wire Rod from Mexico, 67 FR 55800 (August 30, 2002)). In the instant investigation, according to the Petitioners, record evidence clearly demonstrates that the Russian energy market continues to be affected by non-market forces. Therefore, the Department should adjust the Respondents' reported energy costs to address these distortions and ensure the accuracy of the final margin. Failure to exercise this discretion would not only result in the introduction of distortions into the dumping analysis, but would establish precedent limiting the Department's ability to address vestiges of non-market economy (NME) distortions in future cases.

The Petitioners state that the economic evidence on the record⁵ of this case makes clear that electricity and natural gas prices were artificially low during the POI and that the Respondents' reported purchase prices for natural gas and electricity should be adjusted to market level. To corroborate their argument, on January 4, 2005, the Petitioners submitted information relating to what the Petitioners term the "effective nationalization" by the Russian Government of Yuganskneftegaz, the core productive asset of a private Russian oil company, Yukos, which occurred on December 19, 2004. The Petitioners argue that this information demonstrates that the Russian Government is increasing, rather than decreasing, its control of the Russian energy sector, which will result in more non-market distortions.

According to the Petitioners, in the Preliminary Determination, the Department reached incorrect conclusions on the status of the newly-adopted reforms and the magnitude of the multi-levelled distortion in the electricity sector. The Petitioners believe that the Department understated the magnitude of the actual distortions and exaggerated the effect of the measures that were actually in place. The Petitioners cite a World Bank Report,⁶ published in June 2003, which states that the extent of energy subsidies in the economy remains large and that, without economic pricing and complementary restructuring of the sector, the country will be unable to meet the large investment needs in the energy sector. They also cite the 2003 Annual Report of the Unified Energy Services (UES) which shows that UES had financial losses on electricity generation.

The Petitioners claim that Russian Government authorities force UES to keep its tariffs at such low level that they fail to cover both UES' costs of generation and distribution and its capital investment needs. They cite UES' Annual Report which, according to the Petitioners, explicitly recognizes that UES' 2003 tariffs do not allow for an adequate return on investment and do not provide sufficient funds for the full replacement of capital equipment. They also cite the World Bank Report, in which the Bank estimates that the 2002 wholesale electricity prices would have to be increased by 100 percent to reach

⁵ See The Petitioners' July 30, 2004, and November 8, 2004, submissions.

⁶ World Bank, Russia: Development Policy Review, Report No. 26000-RU, June 9, 2003, at ii.

the level of the long-run marginal costs. To calculate the adjustment for the POI, the Petitioners propose to use the 2002 electricity benchmark price from the World Bank Report, inflated either by the actual increase in electricity prices for Avisma and SMW between 2002 and 2003, or by UES' increase in the production costs of electricity over the same period.⁷

The Petitioners further assert that, to accurately estimate the price of electricity that the Respondents would pay in an undistorted market, UES' electricity prices should be adjusted for the distortions arising from the extremely low natural gas prices paid by electricity producers since the majority of the electricity consumed by the Respondents during the POI was generated from natural gas. In response to the Department's concern about how to take into consideration "the role of other non-gas based electricity supply sources in determining whether a significant distortion exists,"⁸ the Petitioners claim that an increase in natural gas prices would be expected to have a high level of "pass-through" into wholesale electricity prices since both demand and supply of electricity are believed to be relatively inelastic (on the supply side, all alternative methods of electricity production, such as coal and hydroelectric plants, are running at capacity; on the demand side, the Respondents have little alternative to electricity since electricity is a major input into magnesium production). As a reasonable basis for estimating the level of increase, the Petitioners suggest using the EU-Russian WTO Accession Negotiations⁹, where the Russian Government agreed to increase the domestic price of gas to specified levels in an effort to achieve the economic goal of covering cost, profit, and investment by the year 2010.

USEC Inc. and United States Enrichment Corporation (collectively USEC) agrees with the Petitioners that the Department must use prices and costs based on meaningful measures of value in every dumping investigation. USEC also emphasizes that the Department recognized in the Graduation Memorandum, that it must proceed cautiously in the treatment of prices and costs in antidumping investigations involving Russian respondents since electricity and gas prices remained subject to government regulation in Russia.¹⁰

In USEC's view, the Department has more than enough information on the record of this case to conclude that Russian energy prices are distorted. Consequently, the Department should adjust the reported energy costs based on the information currently on the record and consider adjustments in future cases, not only with regard to energy, but also to other inputs.¹¹ However, should the adjustment

⁷ See the Petitioners' submission dated January 18, 2005.

⁸ Preliminary Determination at 59201.

⁹ EU, "Russia - WTO: WU-Russia Deal Brings Russia a Step Closer to WTO Membership," Brussels, May 21, 2004, IP/04/673. http://europa.eu.int/comm/external_relations/russia/intro/ip04_673.htm.

¹⁰ USEC's submission dated November 8, 2004.

¹¹ Id.

not be made in this case, USEC states that it is critical for the Department to maintain flexibility on this issue, given that the Department's application of market-economy principles to the Russian Federation is only beginning.¹²

Avisma argues that the Petitioners have not provided any legal basis for rejecting Avisma's energy costs. In Avisma's reading of the statute, the Department is required to calculate costs

based on the records of the exporter or producer of the merchandise, if such records are kept in accordance with the generally accepted accounting principles of the exporting country... and reasonably reflect the costs associated with the production and sale of the merchandise (section 1677b(f)(1)(A)).

Furthermore,

{i}f in the case of a transaction between affiliated persons involving the production by one of such persons of a major input to the merchandise, the {Department} has reasonable grounds to believe or suspect that an amount represented as the value of such input is less than the cost of production of such input, then the Department may determine the value of the major input on the basis of the information available regarding such cost of production (section 1677(f)(3)).

According to Avisma, unless the above exceptions apply, in the market economy context, the Department does not have the authority to adjust reported costs.

With regard to the Graduation Memorandum, Avisma claims that, when the Department determined that Russia had reached market-economy status, the Department explicitly recognized that the bases for disregarding costs and prices in Russia were those already articulated in the statute for all market economies. Avisma believes that the Department, by repeating the words of the statute, was not creating a special rule for Russia; rather, the Department recognized that the market-economy rules (including the subsidy rules) now apply to Russia.

Avisma claims that the Petitioners misstate the law by focusing on the costs of unrelated suppliers rather than the costs of the respondent company itself. According to Avisma, the Petitioners focus on the meaning of the words "associated with" in section 1677(f)(1)(A) of the statute. Avisma argues that the whole phrase "reasonably reflect the costs associated with the production and sale of the merchandise," relates to the costs of the respondent company, not the costs of unaffiliated suppliers. To support its position, Avisma cites the Statement of Administrative Action (SAA) provisions which cover that section of the statute, claiming that the SAA commentary supports the position that the

¹² USEC's submission dated January 18, 2005.

proper legal analysis lies with the costs to Avisma, not with the costs to its suppliers. Avisma also cites a decision by a WTO panel (United States – Anti-dumping Duty on Dynamic Random Access Memory Semiconductors (DRAMS) of One Megabit or Above from Korea, WT/DS99/R (January 29, 1999)), which found that the Department properly disregarded a cost study prepared by outside consultants on behalf of the producer because it did not constitute “records kept by the exporter or producer under consideration” as required by Article 2.2.1.1. Avisma concludes that, for antidumping purposes, it is irrelevant whether Avisma’s supplier is being subsidized, selling at a loss, or is making windfall profits. The only issue the Department needs to determine is whether Avisma’s books and records accurately reflect the costs Avisma actually incurred, which neither the Petitioners nor the Department have disputed.

With regard to the case precedent cited by the Petitioners in which the Department has adjusted or disregarded reported costs, Avisma counters that in each case the Petitioners cite, the adjustment was based upon respondent’s own costs and records. In Avisma’s view, none of the cases cited by the Petitioners offer support for the proposition that the Department can adjust respondent’s costs because of unrelated third parties’ costs. Furthermore, in all cases where cost was disregarded even though the records were maintained in accordance with GAAP, a “distortion” was found in the companies’ accounting practices. Therefore, Avisma argues that the Department does have the authority to make adjustments, but only in instances where an accounting practice is at issue, which they claim is not the case here.

With regard to the EC cases, Avisma argues that the Petitioners’ reliance on EC cases demonstrates the lack of support for their position in the U.S. statute, Department regulations, or case precedent. Furthermore, Avisma claims the EC cases do not say what the Petitioners imply: the two cases cited by the Petitioners were conducted before the EC granted market-economy status to Russia and in neither case did the EC find that the Russian energy prices were per se distorted. Furthermore, in one of the cases, the EC relied upon the reported energy prices of one of the Russian companies.

Avisma claims that the Petitioners have mischaracterized the Graduation Memorandum. Avisma notes that the fact that the Department may give Russian energy prices careful consideration in future trade cases, is in no way a definitive statement that the Department has the legal authority to adjust Avisma’s energy prices in the context of an antidumping case. Avisma points out that the Department specifically refers to “future trade remedy cases.” Avisma argues that this language constitutes intentional phrasing by the Department so as to not state “antidumping” cases. Avisma assumes that energy policies would be dealt with in the context of other types of trade cases, such as CVD or Section 301 cases. Furthermore, Avisma states that the Department noted in the Graduation Memorandum that the continuation of the Russian Government’s current energy price regulatory policies may warrant careful consideration which would only properly be addressed in the context of a countervailing duty (CVD) case. Avisma argues that the courts and the Department have consistently refused to adjust a

company's costs in a market-economy case for alleged subsidies, instructing the petitioners to file a CVD petition instead. A CVD case, therefore, would be the proper forum to address the Petitioners' contention that the Russian Government is subsidizing the cost of energy, thus, causing an alleged "distortion" to the electricity costs of the Respondents.

Avisma further argues that if the Department chooses to analyze the costs of unrelated suppliers, each antidumping case will turn into a complicated forensic accounting exercise. Avisma states that government involvement in the energy sector occurs on some level in every country, including the United States. However, according to Avisma, this type of analysis will inevitably reach beyond energy prices. In fact, Avisma contends that adjusting the energy costs in this case will open "Pandora's Box" and affect every other market-economy case, which will require a review of any price, high or low, on the accusation that it is a "distorted" price. For this reason, the Department's attempts to temper the effects of a holding, so as to limit it to the "unique circumstances" of this case, will not hold water.

With regard to the boundaries of the authority to make adjustments, Avisma points out that, in the Preliminary Determination, the Department stated that it was considering whether it has the authority to examine the cost of inputs into the inputs used in producing the subject merchandise. Avisma argues that the Department is concerned about an alleged distortion in the Russian electricity market which may be caused by the alleged low price of natural gas, which is an input into the production of electricity for certain electricity suppliers. Thus, Avisma argues, the Petitioners fail to address the Department's concern, because, in order to make the adjustment the Petitioners are requesting, the Department must effectively examine the cost of inputs into the inputs.

Avisma claims that the evidence on the record does not support the Petitioners' contention that the Russian energy market is distorted. According to Avisma, the Petitioners have chosen to disregard verified evidence in order to artificially create or magnify any alleged distortion in the Russian electricity market. Avisma points out that in the Graduation Memorandum, the Department noted that no markets are perfect and most have some form of government distortions. Avisma claims that this is especially true of the energy sector where many countries have some form of government control.¹³

According to Avisma, the Russian energy market has changed significantly since the Graduation Memorandum:¹⁴ the price of electricity has increased dramatically over the last several years and a free market for electricity has been created (during the POI), providing the Department with a possible benchmark against which to compare the regulated prices. Avisma states that this is evidence that the reforms in the Russian electricity sector, while incomplete, are having a real impact on the market. As of October 2003, Avisma became eligible to purchase electricity on the open market, as verified by the Department. Avisma argues that Avisma is now free to purchase the cheapest electricity available, which may be coal, nuclear, hydro, or gas generated. Avisma further argues that there is evidence that

¹³ Avisma provided details of government intervention in energy markets in its September 13, 2004, submission.

¹⁴ Detailed information on economic reforms in Russia was submitted in Avisma's September 13, 2004, November 8, 2004, and November 18, 2004, submissions.

any “distorted” prices referenced by the Petitioners are largely the result of rates for residential users, not industrial users. Avisma therefore concludes that industrial users are actually “subsidizing” the residential users.

In support of its assessment of the impact of recent economic reforms, Avisma cites the 2004 Organization for Economic Cooperation and Development (OECD) report which, Avisma claims, tracks closely what has been observed during the opening months of liberalization of the Russian energy sector:¹⁵ prices of electricity in the competitive trading market have declined to the point that the price in that sector is lower than in the regulated sector. The OECD report also states that “while it is clear that Russian electricity tariffs must rise over the long term, they are not obviously low at present.” Therefore, Avisma concludes that, contrary to the Petitioners’ assertions, there is hardly the universally held opinion that Russian electricity prices are grossly distorted or “unfairly” low. According to Avisma, the 2004 OECD report, which is more recent than the World Bank Report cited by the Petitioners, clearly supports the premise that current electricity prices may not be “too low.”

Avisma further notes that past determinations involving Avisma demonstrate that the price paid by Avisma for electricity is not distorted and that the Petitioners’ proposed price increases would be inconsistent with the Department’s own findings.¹⁶ Avisma points out that, in prior investigations the Department consistently gave Avisma the lowest electricity tariffs applied in the surrogate countries selected, as the Department saw Avisma to be a large industrial consumer of electricity. Additionally, Avisma points out that both the Department and the Court of International Trade (CIT) have recognized that large industrial users will pay steeply discounted prices. Thus, Avisma argues, it is illogical, and contrary to Department precedent, to suggest that Avisma’s electricity prices are distorted.

Avisma further argues that the Petitioners have failed to show that the Russian electricity prices do not provide for full recovery of costs. While the Petitioners cite UES’s 2003 financial statement, which states that tariffs “currently do not provide sufficient funds for the full replacement of property, plant and equipment,” Avisma argues that the Petitioners’ reading of this statement is misleading. Avisma claims that the statement cited by the Petitioners is a very general statement made by a huge company with multiple subsidiaries which cannot be used as a reason to find that electricity supplied to a single consumer was sold at a price that does not allow for the full recovery of costs. Avisma concludes that the evidence on the record does not support the claim that for high-voltage industrial users, such as Avisma, the current tariff rates are insufficient to allow the full recovery of the costs of supplying electricity.

¹⁵ OECD Economic Surveys: Russian Federation at 172 (2004), attached to Avisma’s submission dated November 8, 2004 (2004 OECD report).

¹⁶ Notice of Final Determinations of Sales at Less Than Fair Value: Pure Magnesium and Alloy Magnesium from the Russian Federation, 60 FR 16440 (March 30, 1995) and Notice of Final Determination of Sales at Not Less Than Fair Value: Pure Magnesium from the Russian Federation, 66 FR 49347 (September 27, 2001).

Avisma contends that, without concrete evidence, determining the “correct” price of electricity is impossible. Avisma claims that the Petitioners’ rather simplistic analysis ignores the complexities of the energy sector in which there are myriad ways to determine the price of electricity for a particular customer or customer class. Avisma contends that electricity pricing inevitably involves a complex series of trade offs and interactions among stakeholders and discounts are generally given to large energy users. Avisma claims this is not a “subsidy,” but a necessary product of the application of the regulatory model and of negotiations, using market leverage, between supplier and customer. According to Avisma, the Petitioners’ goal of shoehorning the entire Russian energy system into a small chart prepared by the World Bank inevitably fails.

In addition, Avisma argues that it is not clear why electricity prices must allow for full recovery of costs, as the Petitioners claim. Avisma notes that in testimony before the Utah Public Service Commission, U.S. Magnesium did not take the position that the price it pays for electricity must allow its supplier to fully recover its costs; U.S. Magnesium simply claimed that the electricity price it pays must merely make a “contribution” to its supplier’s fixed costs.¹⁷ Avisma concludes that the Petitioners, in this investigation, are setting a standard for electricity pricing that they themselves do not meet because it is clear that U.S. Magnesium’s own electricity tariff does not cover full costs. Avisma highlights the fact that the Russian electricity producers are making a profit, their level of capital investment is greater than their depreciation and it is not universally accepted that current industrial electricity rates are too low to ensure full recovery of costs. Because large industrial users such as U.S. Magnesium and, one assumes, Avisma, need only to make a “contribution” to fixed costs, Avisma argues that no adjustment is needed to Avisma’s energy costs.

Avisma further claims that U.S. Magnesium’s testimony before the Public Service Commission highlights the incredible difficulty in making “correct” costs calculations, even though the amount of information available to U.S. Magnesium is certainly more than what is available to the Petitioners with regard to Avisma and the Russian energy market. On this basis, Avisma questions the accuracy of the margin calculations using the simple World Bank chart, proposed by the Petitioners.

In response to the Petitioners’ argument that the dumping margins should be calculated as accurately as possible, Avisma challenges the accuracy of the various adjustments to the electricity prices proposed by the Petitioners. Avisma notes that the World Bank report used by the Petitioners as the basis for the proposed adjustment was published in June 2003 and shows that even most references to 2002 were preliminary or estimates; therefore, a significant portion of the data was presumably from the NME period.

Avisma rebuts the Petitioners’ contention that the Department should adjust electricity prices for the alleged distortion arising from low natural gas prices paid by electricity producers. Avisma argues that

¹⁷ See also Avisma’s submission dated November 8, 2004.

since 1999, the price of natural gas to industrial users in Russia has increased substantially; based on statistics collected by the OECD for every year since 1999, the rate of increase of the natural gas price to industrial users has exceeded the rate of increase of the producers' price index. Avisma explains that along with the increase in price, the amount of barter payments has almost been eliminated, and the OECD found that any subsidy to industry is shrinking fast and that households, not industries, are receiving the largest share of any gas subsidy. Additionally, Avisma states that the 2004 OECD report reached the conclusion that domestic gas prices are already at or above break-even levels and the effective rate for industry is above the regulated rate because a substantial portion of the gas purchased by the electricity suppliers is outside the regulated sector.

Avisma also takes issue with the Petitioners' conclusion that it is likely that increased natural gas costs would pass through into wholesale electricity prices. First of all, Avisma argues that the prices for natural gas, oil, and coal used by the Petitioners are general averages of the whole industry and, thus, do not take into consideration how a change in price would affect different types of plants, especially those located in different geographic areas. Second, Avisma claims that Avisma can now "switch" to other fuel sources since Avisma has the ability to purchase electricity on the competitive market from several suppliers that rely on a variety of fuels.

Finally, Avisma argues that the estimated increase in natural gas prices proposed by the Petitioners is based on a press release by the European Union (EU) related to closed-door negotiations and the unpublished results of bilateral negotiations between the EU and Russia in connection with Russia's WTO accession. For a benchmark number, Avisma notes that the Petitioners take a simple average of the range of the price concessions for the year 2010. Because the Russian accession process is not yet completed, neither the Petitioners nor Avisma can access the calculations and the underlying assumptions of this price range. Avisma claims that such future price estimates could hardly be considered appropriate for the Department to use in calculating a natural gas price.

Avisma concludes that the Petitioners would have the Department ignore the Respondents' own verified record evidence and use instead estimates made before the POI and projections as to what prices should be in future years - as late as 2010. According to Avisma, should the Department make an adjustment in this case, the Department should be absolutely certain that the price at issue is in fact unreliable and distorted. Avisma claims that the Petitioners have not been able to place on the record anything which shows with absolute certainty that the price paid by Avisma to its electricity supplier is distorted. On the contrary, Avisma claims that the costs used by the Petitioners are estimates based on dated information and a series of unprovable assumptions. As such, they should be rejected.

In response to the Petitioners' submission of information pertaining to the auction of Yukos' main productive asset, Avisma states that the Russian Government's intervention with Yukos is a tax and

criminal issue conducted by a sovereign nation and is not a property issue.¹⁸ Additionally, Avisma argues that such intervention has had little negative effect on foreign investment which continues to increase (including investment by Western oil companies). Avisma argues that state ownership of the oil sector has little effect on the nature of a market economy overall and that other market economies have state-owned oil sectors. Avisma concludes that the Yukos litigation does not diminish the fact that Russia is in the midst of economic reforms and liberalization.

In its January 18, 2004, submission, Avisma takes issue with the Department's statement in its Energy Memorandum that any adjustment to Russian energy prices would be a "technical adjustment."¹⁹ Avisma claims that an adjustment to reported costs in this case, notwithstanding the Department's language, would be read as a policy decision implying that the Department will accept the verified energy prices of every market-economy country in the world, except Russia, because the Department has concluded that the Russian energy sector is distorted. Thus, according to Avisma, any such adjustment would be clearly policy-based.

In refuting the Petitioners claim that this case is unique because energy represents a "significant input" in the cost of magnesium, Avisma argues that every case involves significant inputs, be they raw materials, energy, or labor, and the law cannot be so narrowly defined as to only include energy. Avisma additionally refutes the Petitioners' claim that this case is unique because energy was specifically mentioned in the Graduation Memorandum. Avisma argues that the simple mention of the issue of energy in the Graduation Memorandum does not expand the Department's authority to give it something not previously granted by the statute.

Like Avisma, Alcoa also argues that the Department does not have the legal authority to make an adjustment to the Respondents' reported and verified energy costs. In its submission of January 14, 2005, Alcoa claims that section 773(f)(1)(A) of the Act and the SAA clearly provide that costs are "normally" calculated based on the records of the exporter or producer of the merchandise and the exceptions to this requirement do not relate to the circumstances of this case. Alcoa claims that the discretion accorded to the Department by the use of the term "normally" in this context is plainly limited to situations where, for example, a respondent's costs are not appropriately allocated. Furthermore, Alcoa claims that the statute makes clear that the relevant consideration is the cost to the respondent company, not the cost of unrelated suppliers, which is what is currently at issue. According to Alcoa, the Petitioners are attempting to incorporate elements of an NME dumping analysis and a subsidy analysis into a market- economy dumping case, and there is no legal base for either approach.

Alcoa agrees with Avisma that the Department has no factual basis on which to adjust for energy costs

¹⁸ See Avisma's January 14, 2005, submission.

¹⁹ Memorandum to the File from Lawrence Norton, Economist, Import Administration, Energy Pricing in the Antidumping Investigation on Magnesium from Russia (January 12, 2004) (Energy Memorandum)

in this case.²⁰ According to Alcoa, the Petitioners have not placed on the record information supporting their claim that the Russian electricity market is distorted. In Alcoa's view, there is substantial evidence on the record that actually contradicts Petitioners' claim and the information on the auctioning of Yukos is insufficient and irrelevant. Thus, the Department has no factual basis to make the adjustment. If the Department were to make the adjustment, Alcoa claims that the Department would be establishing a dangerous precedent, which will have a significant impact on virtually all of its other antidumping cases, because there is nothing unique about this case that will distinguish it from other cases.

SMW argues that the Department should continue to rely on the Respondents' reported energy costs as it did in the Preliminary Determination for all the reasons contained in the Respondents' prior submissions.²¹ SMW claims that the verification report refutes the Petitioners' allegation that government involvement has distorted downwards energy prices, since it states that the prices in the unregulated electricity market tend to be lower than the prices in the regulated market. According to SMW, after the thorough cost verifications of the Russian Respondents and despite the Petitioners' additional submissions, the record still supports the Department's original decision.

In its January 21, 2004, submission, SMW states that the 2003 electricity rates reported by SMW and verified by the Department, are not significantly different from the rates in the reports cited by the Petitioners and the Department, and therefore they are not "significantly distorted." On the issue of the "technical adjustment," SMW comments that given the Russia-wide nature of the electricity costs calculated by the World Bank and the OECD, addressing past, present, and future Russian energy policy on a national basis, it is difficult to see how any adjustment could not be viewed as a policy decision. According to SMW, the same rationale would also apply to other Russian industrial consumers of electricity.

The Petitioners rebut Avisma's interpretation of the statute by stating that 1) the statute provides that the calculation of costs is "normally" based on respondent's books and records when two criteria are met: the reported costs a) are GAAP consistent and b) reasonably reflect the costs associated with the production and sale of the subject merchandise; 2) the qualifying term "normally" indicates that there are circumstances in which the Department will not calculate costs based on respondent's records; 3) Avisma attempts to combine two independent statutory criteria to assert that, as long as a company's records are maintained in accordance with GAAP, the costs recorded in those records reasonably reflect the costs associated with the production and sale of the subject merchandise; 4) the Graduation Memorandum specifically recognizes the Department's authority to make this adjustment; and 5) the Department has a longstanding practice of disregarding or adjusting reported costs when they do not reasonably reflect the costs of production and sale of the subject merchandise.

²⁰ See Alcoa's January 14, 2005, submission.

²¹ SMW here cites its own submission of September 15, 2004, and to Avisma's submissions of September 1 and September 13, 2004.

In response to Avisma's argument that the Department cannot assess whether an input cost is distorted if the input was acquired from an unrelated supplier, the Petitioners state that there is no prohibition in section 773(f)(3) of the Act (the major input rule) preventing the Department from examining distortions in the cost of inputs except when dealing with an affiliated supplier. According to the Petitioners, the language of the statute permits the Department to consider whether the costs reasonably reflect the costs "associated with" the production of the subject merchandise. The Petitioners claim that, under the plain meaning of the statute, an input cost, such as energy, is clearly "associated with" the production of the subject merchandise and may be reviewed by the Department. The Petitioners further argue (in their January 21, 2004, submission) that Avisma and Alcoa's reading of the statute combines the Department's broad authority under section 773(f)(1)(A) of the Act with the separate provision of 773(f)(3), the major input rule, stating that the Department cannot adjust a respondent's distorted energy input costs unless the respondent obtained the input from an affiliated supplier. In the Petitioners' view, nothing in the statutory scheme indicates that section 773(f)(3) of the Act should be read to limit the Department's broad authority under section 773(1)(A) with respect to adjustments to respondent's costs under certain circumstances.

In the same January 21, 2005, submission, the Petitioners also state that Avisma and Alcoa's interpretation of the SAA is incorrect. Specifically, the Petitioners state that the language of the SAA that Avisma and Alcoa cite does not state that Congress intended to limit the Department's discretion to adjust costs only to situations where respondents have improperly allocated costs. The Petitioners argue that the language of the SAA discusses the improper allocation of costs as nothing more than one example of many circumstances where a respondent's reported costs may not reasonably reflect the costs associated with the production of the of the subject merchandise, rather than the only instance where the Department may adjust.

In response to Avisma's concern that an adjustment to Russian energy costs may open a "Pandora's box" whereby each dumping case "will turn into complicated forensic accounting exercises," the Petitioners claim that there are sufficiently unique circumstances in the instant case that preclude establishing a precedent that the Department determine distortions for every input in every future case. These circumstances include Russia's recent graduation to market-economy status, the fact that the Department has identified the possibility of price distortions in the Graduation Memorandum, and the fact that energy represents a significant input in the production of magnesium metal, including both electricity and natural gas, which accounts for 68 percent of the fuel for all UES thermal generation of electricity. Thus, in the Petitioners' view, the boundaries of application of the required adjustment are very narrow.

With regard to Avisma's contention that if the Russian energy sector is subsidized, the appropriate forum for the Petitioners' concern is a CVD proceeding, the Petitioners argue that they are not asking the Department to make a determination that the Russian Government is subsidizing the energy sector. They are asking that the Department, in calculating costs to determine whether magnesium from Russia

is being sold at less-than-fair value (LTFV), make the necessary adjustment to eliminate the existing distortions, so that the Respondents' costs reasonably reflect the costs associated with the production and sale of the subject merchandise. The Petitioners rebut Avisma's contention that, in cases where a country's GAAP are followed, the Department has only adjusted cost when there was a problem with the accounting practices. In support of their argument, the Petitioners point to the Department's Antidumping Duty Manual, which states that the Department will adjust reported costs to eliminate distortions in countries experiencing high inflation.²² To support this argument the Petitioners also cite the Notice of Final Determination of Sales at Less Than Fair Value: Silicomanganese from Venezuela, 59 FR 55436 (Nov. 7, 1994), the Graduation Memorandum, and Cut-to-Length Steel Plate From Russia. The Petitioners add that they could not obtain relief by filing a CVD case because they would not be able to demonstrate that the subsidy is specific, given the pervasiveness of the government control of the energy sector.

The Petitioners also take issue with SMW's observation on the pricing differences between the regulated and unregulated Russian energy markets. The Petitioners note that SMW's assertion does not take into account important record information relating to the "unregulated" electricity market and to Russia's plan for future energy sector deregulation. With regard to the unregulated market, the Petitioners claim that 1) it was not in place for 10 of the 12 months of the POI, 2) it is a spot market and therefore reflects only short-term cost and price factors, 3) sellers limit their sales to 15 percent of their production on this market, 4) it includes electricity provided by nuclear and hydroelectric generators, who have low short-run marginal costs compared to the thermal power generators (such as natural gas), and 5) buyer participation is limited. Therefore, the Petitioners claim that the fact that the unregulated market price is lower than the regulated prices does not indicate that Russian electricity prices were undistorted during the POI. With regard to future deregulation of the Russian energy sector, the Petitioners claim that recent developments raise serious concerns as to whether the deregulation of this sector will in fact take place as planned. The recent sale of Yukos' primary production assets seems to indicate that of the three segments of the Russian sector - oil, natural gas, and electricity - the initial privatization steps in oil and natural gas segments have not only been halted, but they have also been reversed.

With regard to Avisma's argument that the Petitioners have attempted to impose a standard of electricity pricing on the Respondents that the Petitioners themselves do not meet, the Petitioners state that Avisma's characterization of the Petitioners' electricity costs is untrue and that the price that the Petitioners pay for electricity simply has no legal bearing on determining the appropriate dumping margin for the Russian producers of magnesium.

The Petitioners also disagree with Avisma's reading of the 2004 OECD report on the conditions of the Russian energy sector. According to the Petitioners, the OECD does recognize the transitional adjustments that will be necessary for the Russian electricity sector to become a sustainable market-oriented operation. The Petitioners claim that the OECD recognizes that in the immediate term, the

²² Import Administration Antidumping Manual: Training/Operating Guide, ch. 8, p.84 (rev. Jan. 1998)

UES' system is in poor physical condition with redundant inefficient operations and that Russian electricity tariff rates must rise over the long-term "to make investment in new generating capacity attractive."

Department's Position:

The Department agrees with the Petitioners that, under certain circumstances, the Department possesses the legal authority to use some reasonable alternative to the costs recorded by the respondents in their books and records in order to calculate the respondents' cost of production. While such adjustments are permissible, the Department has determined that, based on the specific facts of this case, for purposes of this final determination, the Department will not disregard or make adjustments to the Respondents' reported electricity costs. The Department's analysis and reasoning are fully explained in the "Energy Costs" section in the Federal Register Notice of Final Determination.

Comment 3: Barter Sales

SMW argues that home-market "barter sales," excluded from the margin calculations for the Preliminary Determination, should be included in the Department's margin calculations for the final determination. SMW argues that these home-market sales are not actually barter transactions, but represent instead the offsetting of the company's accounts payable with outstanding accounts receivable. SMW notes that the prices of barter sales were consistent with the prices stated in the contracts and that these sales were treated basically the same as cash sales in the accounting system. SMW also notes that barter sales were made at comparable prices to non-barter sales of the same product, and that when comparing sales made to the same customer over the same time period, prices for barter and non-barter sales are identical. SMW claims that averaging prices over the POI yields a price difference because this method does not account for changes in price over time.

The Petitioners agree that the Department should include both Respondents' barter transactions in its margin calculations for the final determination. The Petitioners argue that these sales are made in the ordinary course of trade. The Petitioners note that both Respondents have provided the Department with sufficient information to ensure that barter and non-barter prices are aligned, that barter prices are linked to market values, and that the Respondents treat barter and cash transactions identically.

Department's Position:

In the Preliminary Determination, citing the novelty of this issue, the Department stated that it would need to collect more information before being able to accurately determine whether "barter" sales were appropriate for use in calculating normal value. As the result of questionnaires issued after the

Preliminary Determination, and as a result of verification, the Department now has sufficient information on the record to determine that these sales are appropriate for use in the calculation of normal value.

The Department learned at verification that, except for a small percentage of Avisma's sales, both companies enter these transactions with the expectation that they will be paid in cash. The various types of transactions that have been referred to as "barter" transactions throughout this investigation involve merely an offset of accounts receivable with accounts payable, not an offer to exchange goods for other goods. Thus, when the Respondents enter these offset transactions, they follow the same procedure as they would with any ordinary cash transaction in terms of valuing magnesium sold and the goods purchased. Therefore, there is no reason to believe or expect that prices for these transactions are not aligned with the prices of "cash" transactions, or that adequate compensation is not received in return for the magnesium sold. We note also that Russian law allows for such offsets, and that the Department reviewed the accounting procedures for these sales which involved simple, transparent, credits to accounts receivable and debits to accounts payable.

With regard to the small percentage of Avisma's sales in which it entered the transaction knowing that it would be compensated with goods, the Department met with members of Avisma's procurement department specially tasked to review these transactions to ensure that reasonable values were assigned to the goods received in exchange for magnesium. These personnel reviewed the value assigned to the goods received in exchange for magnesium in the same manner they reviewed the price paid for goods purchased by Avisma in any other transaction.²³ As we state in the Avisma Verification Report²⁴ at pages 13-14 (references omitted):

The Revision Department maintains a database of prices previously paid for the same merchandise and current market prices, which are periodically confirmed through market research. Avisma told us that if the price of the bartered merchandise is deemed excessive, the Revision Department may reject the transaction.

Thus, the concerns highlighted in the Preliminary Determination have been adequately addressed and we believe that these "barter" sales are properly included in the calculation of normal value.

Comment 4: Sales Through Bonded Warehouse

²³ Avisma had one contract covering goods-for-goods exchanges that were not reviewed by this arm of the procurement department. However, these sales have been excluded from the margin calculations for failing the "arm's-length test."

²⁴ See Memorandum to the File, from Sebastian Wright Through Maria MacKay; Magnesium Metal From The Russian Federation: Verification Report for JSC AVISMA Titanium-Magnesium Works, December 23, 2004 (Avisma Verification Report).

Avisma argues that certain U.S. sales of subject merchandise should be excluded from the Department's calculations. Avisma claims that during the POI, it sold subject merchandise to its affiliate, Tirus, U.S., Inc. (Tirus), who had reason to believe the goods were being sold by its customer, a trading company, to another country. Avisma states that the product was sold duty-unpaid because, given the final destination, it would have been illogical to enter the product into U.S. commerce due to the high rates of duty on magnesium. Avisma further states that the trading company told Tirus that the merchandise was being sold to another country. Additionally, U.S. import statistics show a difference between general imports and imports for consumption, which, Avisma argues, suggests that products entered in-bond in the United States were not subsequently entered for consumption in the United States. Avisma further states that the ultimate purchaser sent an e-mail to Tirus confirming that no Avisma products it received from the trading company entered the United States during the POI.

Avisma states that there is no evidence that the sales to this trading company entered U.S. commerce. On the contrary, the record shows that the same final purchaser was also listed on invoices for sales made to a third country even though the address listed on the invoice was a U.S. address. Avisma claims that neither Avisma nor Tirus knew the ultimate destination of the product at the time of the sale. Avisma argues that in the two previous investigations (1995 and 2001)²⁵, the Department found no reason to impute knowledge of the ultimate destination based on the circumstances of the sales transactions. In 2001, the Department found that the mere fact of listing a U.S. address on the sales document to a reseller does not amount to knowledge that the product was destined for ultimate use in the United States.

According to the Petitioners, these sales were delivered to a U.S. port, whether in bond or not. Therefore, the burden is on the Respondent to affirmatively demonstrate that the merchandise was moved from the U.S. port to a non-U.S. destination. The Petitioners state that Avisma does not claim that it has affirmative evidence that the merchandise delivered from Russia to the U.S. port was in fact re-exported to another country. At verification, the Department confirmed that Tirus also does not have affirmative evidence of re-exportation.²⁶ Furthermore, the Petitioners note that Tirus' customer has locations in both the United States and a third country. For these reasons, the Petitioners argue, the Department should reject Avisma's argument that it is reasonable to believe that the destination of these shipments was outside the United States.

Department's Position:

We agree with the Petitioners that the sales in question should be included in Avisma's U.S. database.

²⁵ Final Determinations of Sales at Less Than Fair Value: Pure Magnesium and Alloy Magnesium From the Russian Federation, 60 FR 16440 (Mar. 30, 1995) and Final Determination of Sales at Not Less Than Fair Value: Pure Magnesium From the Russian Federation, 66 FR 49345 (Sept. 27, 2001).

²⁶ Memorandum to the File, from Sebastian Wright and Mark Hoadley; Magnesium Metal From The Russian Federation: Magnesium Metal From The Russian Federation: Verification Report for JSC AVISMA Titanium-Magnesium Works, December 29, 2004 (Tirus Verification Report).

Avisma admits that it does not know the ultimate destination of these sales. While Avisma argues that the facts support the conclusion that these sales left the United States, the Department cannot exclude such sales from the U.S. database because: 1) the Respondent did not know at the time it made the sales to a U.S. customer that the merchandise would leave or not enter the United States; and 2) there is no definitive proof that the merchandise in fact did leave or did not enter the United States, with or without the Respondent's knowledge.

Our position in this case is consistent with similar determinations in prior investigations. For example, in the 2001 magnesium investigation, Avisma's merchandise was shipped to the United States without Avisma's knowledge. We determined not to include those sales in the U.S. database. Avisma excerpts the following statement by the Department in that investigation, which it claims is inconsistent with the Department's current position:

In fact, we found that Greenwich shipped to non-US destinations in the ordinary course of its business. As at Avisma's verification, the Department again found no evidence that Avisma knew or should have known that the merchandise purchased by Greenwich from a third-country reseller was destined for the United States.

See Final Determination of Sales at Not Less Than Fair Value: Pure Magnesium from Russia, 66 FR 49347 (Sept. 27, 2001) and accompanying Issues and Decision Memorandum, at Comment 3.

In that decision, the Department determined that Avisma's merchandise resold in the United States from a third country should not be considered as part of Avisma's U.S. sales because Avisma did not have knowledge at the time of its sale to the third-country customer that the goods were to be shipped into the United States. In this case, we determined that the sales at issue should be considered U.S. sales because, at the time of sale from Tirus' U.S. warehouse to a U.S. customer, Tirus did not have knowledge that these goods would leave or not enter the United States.

We note that in this investigation, we are classifying as non-U.S. sales only those sales that Tirus made with knowledge that the merchandise would be shipped in bond from the United States to a specified destination outside the United States. In contrast, there is no evidence that the sales in question left the United States or never entered the country. Avisma has submitted one e-mail (dated well after the POI) from the customer of Tirus' customer that Avisma claims confirms that the merchandise in question did not enter the United States during the POI. However, this e-mail does not demonstrate that Tirus knew that the destination of the merchandise in question was a country other than the United States nor that this merchandise in fact was shipped to a destination outside the United States.

Finally, we disagree with Avisma's claims that statements by the Department in the Preliminary Determination concluded with certainty that these sales entered U.S. customs territory. Our intention was to conclude that absent definitive evidence to the contrary, we must assume that merchandise sold out of the U.S. affiliate's warehouse to a U.S. customer and billed to a U.S. address entered U.S. customs territory.

Comment 5: Model Matching of Certain Avisma Products

Avisma argues that the Department used an incorrect home-market model when matching certain sales made in the United States. Avisma argues that the statute, court precedent, and the Department's past practice mandate that model matching be based on physical characteristics. The CIT has stated that when identical merchandise is not available, the Department must select similar comparison merchandise based on the physical characteristics of the merchandise being compared, and that products must be as similar as possible to ensure the accuracy of the antidumping margin calculations. Avisma argues that the Department instead ignored the physical characteristics of the products at issue, which resulted in U.S. sales being matched to a home-market model that is not the most similar based on physical characteristics.

Avisma argues that the home-market product that the Department chose to match to the U.S. product in question is not the most similar merchandise because it was selected based on specification labels (conformity with ASTM standards) rather than on the chemical characteristics of the product. Avisma states that another type of magnesium sold in Russia is closer to the product it sells in the United States, in all aspects other than in level of tolerance for impurities. Furthermore, the alternative product sold in Russia is also used in similar applications, *i.e.*, the automotive industry. Therefore, the Department should use this product for its model match.

Avisma also argues that the home-market sale of the product chosen by the Department is outside the ordinary course of trade because it is not a "normal" sale, as required by the statute, in that the sale was of a minuscule amount, sold to only one customer in a niche market, with a promotional quality. Avisma argues that if the Department does not find this sale to be outside the ordinary course of trade, the Department would encourage manipulation in future cases by allowing companies to circumvent the antidumping order by making select sales of a product at controlled prices.

The Petitioners argue that Avisma's complaints regarding the model match methodology should be rejected because Avisma failed to submit in a timely manner a complete and comprehensive discussion of the methodology it believes should be applied in determining the most appropriate grade match. The Petitioners note that the Department requested comments on model matching criteria on March 26, 2004, but Avisma responded that it did not have any comments at that time, and did not raise the issue until verification. Furthermore, the Petitioners state that Avisma's analysis is incomplete because it did not take into account all grades sold in the home market. In addition, Avisma failed to rebut the Department's findings at verification that the products matched have similar end uses. Therefore, the Petitioners argue, the Department should ignore Avisma's proposal.

Finally, the Petitioners argue that the home-market sale that the Department used as a match for U.S. sales in the Preliminary Determination is not outside the ordinary course of trade, as there is nothing extraordinary about its sales terms with respect to price, quantity, and profit margin.

Department's Position:

We disagree with Avisma's argument that another home-market product would provide a more appropriate match to the U.S. sales of alloy magnesium in question. The Department issued a letter to all interested parties proposing model match criteria and a hierarchy on March 26, 2004, and asked all parties to submit comments by April 1, 2004. Avisma responded by stating that it did not have any comments at that time. In fact, the Department did not learn of any concern with the proposed model match until verification during the week of October 25-29, 2004, seven months after our request for comments. It is obvious from the letter we issued containing the model match proposal and the subsequent questionnaires issued that whether a product "conformed" to ASTM standards would be central to product matching. Because of the late timing of these comments, we did not have an opportunity to question Avisma about its alternative model match proposal. Nor did other parties in this case have an opportunity to submit questions to the Department on Avisma's proposed changes. Thus, we believe there is a reasonable basis for rejecting Avisma's model match argument on timeliness alone.

Aside from the timeliness concern, we also disagree with the substance of Avisma's arguments. Avisma stresses that the Department is required to match products on the basis of physical characteristics, but never explains why national standards cannot be considered to incorporate physical characteristics, nor does it ever mention the numerous antidumping duty orders issued by the Department on steel products that have included in the model matching hierarchy a characteristic for national standards. Avisma's arguments appear to imply that national standards governing alloy magnesium production are unimportant, or at least so unimportant compared to chemical content that the relative priority of those criteria in the hierarchy does not need to be discussed. Avisma simply states that alloy products should be matched strictly according to the similarity of their chemical content, without any explanation as to why this is so.

While undoubtedly ASTM and non-ASTM conforming products can be used interchangeably to some degree, business-proprietary information on the record demonstrates persuasively that whether a product conforms to ASTM, GOST, or some other standard, is a significant fact differentiating alloy magnesium products (as opposed to pure magnesium products) in the minds of customers. See Avisma Final Analysis Memo at 1.

We do not agree with Avisma that its sale of the home-market product used for matching purposes is outside the ordinary course of trade. Avisma's argument rests on what it characterizes as the "promotional quality" of the product, what it characterizes as the "niche market" for this product, and on the limited quantity of that product sold in the home market. While we agree with Avisma that the quantity delivered was less than other home-market sales, we do not believe that the quantity was so small as to indicate that the sales are "extraordinary" for the market in question or involve "unusual terms of sale." 19 C.F.R. 351.102 (b). In fact, the sales quantity appears significant and we were able to identify numerous other sales in the home-market database of similar quantities, including numerous other sales of the product Avisma proposes we use as a match for its U.S. alloys. See Avisma Final

Analysis Memo at 1. The record evidence indicates that Avisma is familiar with the home-market product in question and would be able to price it appropriately. We also see no connection between Avisma's statement that "Russian customers generally purchase goods using GOST standards" and its conclusion that "therefore . . . this sale had a promotional quality to it." We note, however, that this statement supports our conclusion that national production standards are not irrelevant to model matching. Avisma also points to differences in the profit rate between the product we used for matching and the product it would like us to use. While we believe the proper comparison would have been between the profit rate of the product, which Avisma argues is outside the ordinary course of trade, and Avisma's magnesium profit rate in general, we find that the profit rate for the product used is not unusual and does not indicate that the price charged for this sale is anomalous. Finally, we agree with the Petitioners that if in the future a party attempts to use small quantity sales to take advantage of the Department's model match criteria and manipulate its dumping margin, the Department can act at that point in time to address such a situation.

We note that, if an order is issued pursuant to this investigation, parties are welcome to raise the model match issue in any future administrative reviews of the order. See Certain Steel Concrete Reinforcing Bars From Turkey: Final Results and Partial Rescission of Antidumping Duty Administrative Review, 67 FR 66110 (October 30, 2002) and accompanying Issues and Decision Memorandum at Comment 1 ("{I}t would be unfair to refuse to make better comparisons which capture differences that are meaningful on a commercial level While it is not our practice to reexamine an established model matching hierarchy in each segment of a proceeding, we will reexamine it if a valid issue is raised by one or more of interested parties.").

Comment 6: Constructed Export Price (CEP) Offset

Avisma argues that the Department incorrectly compared the level of trade (LOT) of Avisma's home-market sales to Avisma's unadjusted U.S. sales, rather than to CEP in order to determine whether home-market and U.S. sales were made at the same LOT. Avisma claims that evidence on the record shows that Russian sales are in fact at a more advanced LOT than the CEP sales. Avisma states that it is not possible to calculate an LOT adjustment to compensate for the difference in LOT because there is no comparable LOT in the home market. Avisma claims that failure to allow the CEP offset will result in a distorted comparison of U.S. and home-market prices.

The Petitioners argue that the Department should maintain its preliminary conclusion that Avisma's sales in the home market and its sales to Tirus, its U.S. affiliate, are at the same LOT. The Petitioners provide an analysis of several selling functions using information from the verification report. The Petitioners claim that these selling functions are performed substantially in the same manner for both home-market sales and sales to Tirus. The Petitioners note that the Department has issued a number of recent determinations in which it denied a CEP offset because the record showed only minor differences in selling activities in each market (see, e.g., Polyethylene Terephthalate Film, Sheet, and Strip from Taiwan, 69 FR 50166 (August 13, 2004)) and the CIT had recently affirmed a denial on that basis. See Corus Staal v. United States F. Supp. 2d 1253, 1270-71 (CIT 2003).

Department's Position:

We disagree with Avisma that a CEP offset is warranted. In accordance with section 351.412(f)(1)(ii) of the Department's regulations, the Department must first find that normal value is at a more advanced LOT than the CEP sales before granting a CEP offset. According to section 351.412(c)(2) of the Department's regulations, in order to make this initial finding, the Department "will determine that sales are made at different levels of trade if they are made at different marketing stages (or their equivalent). Substantial differences in selling activities are a necessary, but not sufficient, condition for determining that there is a difference in the stage of marketing." Thus, as the Petitioners claim, the Department must find significant differences in selling functions before granting the offset.

According to Avisma, "the only activities arguably related to sales to the end customer remaining at the CEP LOT are order processing and freight and delivery services to send the materials to the United States. These constitute little more than logistical inter-company transfer services, not the advanced selling services performed by Avisma in the Russian market." Avisma's attempts to downplay the logistics involved in shipping magnesium from Russia to the United States, sometimes through a third country, however, are not supported by the evidence on the record. In addition to shipping-related functions, there are many other selling functions involved. These functions are:

1. Technical Services: Avisma personnel made statements that they provide a low level of technical services to both markets. These personnel stated that Tirus would be able to answer most questions itself, and that most of its home-market customers were also familiar with the technical aspects of the products. See Avisma Verification Report at 12.
2. Sales Processing: The Department verified that Avisma maintains sales and accounting personnel who work interchangeably for sales to both markets (although some sales personnel are tasked specifically to domestic sales). While Avisma emphasized at verification that domestic sales involve more work given the wide variety of both quantities sold and customers compared to the U.S. market, and the need for prepayment. See Avisma Verification Report at 12. Nevertheless, some level of processing is still involved in making sales to Tirus (see item number 5 below regarding Avisma's sales negotiations with Tirus).
3. Freight Handling: As noted above, shipping to the United States appears more complex than Avisma claims. As noted by the Petitioners in their rebuttal brief, business proprietary information suggests that U.S. sales involve more complex operations than home-market shipments.
4. Inventory Maintenance: Avisma claims that it maintains an inventory for its domestic customers. However, domestic inventory expenses are not significantly different than export inventory expenses. Moreover, Avisma does not reference anything on the record to support its assertion other than the fact that it has spot sales in the home market and not in the United States.

5. Sales Forecasting and Research: While Avisma negotiates long-term “contracts” with its home-market customers for planning purposes (see Avisma Verification Report at 6), as we learned at the verification of Tirus:

Tirus US said that near the end of each calendar year it begins negotiations with Avisma for allocations of magnesium for the following year. . . . Tirus US personnel travel to Russia and negotiate an allocation of Avisma’s capacity to meet this demand. Tirus US takes the vast majority of Avisma’s capacity . . . and meeting the North American demand is a priority for Avisma’s capacity. Once negotiations are completed and the transfer price agreed upon, Avisma and Tirus US enter into annual agreements for shipments to the United States. Different contracts might be concluded for different types of metal, different destinations, and different transfer prices.

See Tirus Verification Report at 3.

Thus, Avisma has planning responsibilities arising from negotiating its U.S. long-term contracts as well.

The record reflects that Avisma’s selling functions exclusive to the home market are limited to the operations involved in completing barter sales (see, e.g., Avisma’s review of the prices assigned to goods received in exchange for magnesium, discussed in the Avisma Verification Report at 13), dealing with more frequent sales to its Russian customers, and accounting for prepayment. These differences do not constitute the “substantial differences” required to find a more advanced home-market LOT. Therefore, we continue to find that a CEP offset is not warranted.

Comment 7: Payment Dates for Certain Home-Market Sales

The Petitioners argue that the Department should correct an apparent error in Avisma’s sales database where some observations have payment dates after shipment dates even though the payment term for those sales is reported as “prepayment.” The Petitioners argue that the Department should replace the reported payment date for those sales with a payment date based on those prepayment sales with payment dates reported correctly.

Department’s Position:

The Petitioners are correct in noting that a number of payment dates reported in the home-market sales database are after the shipment date, even though the payment terms for those sales are labeled as “prepayment.” As we noted in the Avisma Verification Report, in certain prepayment sales, Avisma receives a partial payment before shipment and the balance after shipment. As explained in the report, Avisma reported the date it received the balance of the payment as the date of payment. This resulted

in the apparent discrepancy among payment date, shipment date, and payment terms, and thus a resulting overstatement of credit expense.

In addition to the discrepancies affecting prepayment sales, the Department discovered at verification several other errors in the reporting of payment dates, ranging up to over a year difference between the actual payment date and the date reported to the Department. See Avisma Verification Report at 18. Avisma provided several different explanations for how the mistakes might have occurred. These explanations all involved prepayment sales. However, the mistakes involved both prepayment and non-prepayment sales. Avisma also recognized that these incorrect dates might have been simply the result of data entry errors. Id. Pursuant to section 776(a) of the Tariff Act of 1930, as amended (Act), the Department may resort to facts otherwise available when the “necessary information is not available on the record,” or an interested party provides information “but that information cannot be verified” The errors in reporting payment dates discovered at verification call into question the accuracy and reliability of Avisma’s payment dates. We therefore determine that the payment dates reported cannot be verified. Accordingly, we find it appropriate to rely on partial facts available to determine payment date.

Section 776(b) of the Act provides that the Department may apply an adverse inference in selecting from the facts otherwise available when “an interested party has failed to cooperate by not acting to the best of its ability” Regarding this standard, the U.S. Court of Appeals for the Federal Circuit has stated:

While the standard does not require perfection and recognizes that mistakes sometimes occur, it does not condone inattentiveness, carelessness, or inadequate record keeping. It assumes that importers are familiar with the rules and regulations that apply to the import activities undertaken and requires that importers, to avoid a risk of an adverse inference determination in responding to Commerce's inquiries: (a) take reasonable steps to keep and maintain full and complete records documenting the information that a reasonable importer should anticipate being called upon to produce; (b) have familiarity with all of the records it maintains in its possession, custody, or control; and (c) conduct prompt, careful, and comprehensive investigations of all relevant records that refer or relate to the imports in question to the full extent of the importers' ability to do so.

Nippon Steel Corp. v. United States, 337 F.3d 1373, 1382 (Fed. Cir. 2003). The CIT has stated, “The requirement that Commerce find the respondent did not comply ‘to the best of its ability’ at least implies a duty on the respondent to make its response reasonably accurate.” Acciai Speciali Terni S.p.A. v. United States, 142 F. Supp. 2d 969, 989 (CIT 2001) (AST).

In Notice of Final Determination of Sales at Less Than Fair Value: Stainless Steel Sheet and Strip in Coils From Italy, 64 FR 30750 (June 8, 1999), the respondent submitted a database at the request of the Department. At verification, the Department found numerous discrepancies between the database submitted and the company’s records. The Department found that a reasonable check of this database

by company officials prior to verification would have alerted the company to the errors (64 FR at 30760). The CIT affirmed the Department's use of adverse facts available, stating, "At verification Commerce was able to identify many of the errors using only the information available to {the respondent and its U.S. affiliate}." AST, 142 F. Supp.2d at 988. The court continued, "Had {the respondent} checked the data submitted, it could have identified errors and corrected them. It did not." Id.

The situation is similar here. Avisma did discover one incorrect payment in the course of preparing for verification, a rather large error, which it reported as a minor correction prior to the start of verification. During verification, however, the Department found numerous other errors, some also significant in size, using only information available to Avisma. We determine that Avisma had the ability to conduct a more thorough evaluation of its own records prior to verification, and discover these errors on its own. Had Avisma done so, it would have been alerted that there was a problem with the method it used to collect and report payment dates. Moreover, Avisma could have reported these problems to the Department before the start of verification. Having failed to do so, the Department finds that Avisma failed to cooperate to the best of its ability, and the application of an adverse inference is warranted.

As a result, the Department has determined that it is appropriate to replace the payment dates reported by Avisma with the longest verified period between payment date and shipment date for prepayment sales (regardless of whether the payment was received in one or multiple installments), and the shortest verified period between payment date and shipment date for all other sales.

Comment 8: By-Product Credit

The Petitioners argue that the Department should recalculate Avisma's by-product credit for chlorine transfers and disposals. The Petitioners assert that Avisma assigns "ownership" of the chlorine gas moving between the magnesium and titanium plants, and from both plants to the disposal facility, on the basis of relative production quantities. The Petitioners point out that the Avisma Verification Report shows that the decision as to which workshop's chlorine gas is disposed of (i.e., magnesium or titanium) appears to be an arbitrary one. The Petitioners contend that given the fact that only the magnesium workshop generates a surplus of chlorine gas, Avisma's gas flows do not reflect the physical reality of the production processes at the magnesium and titanium workshops.

The Petitioners maintain that there is no reason for the titanium plant to receive chlorine gas from the magnesium plant while it disposes of chlorine gas itself. Instead, the Petitioners assert, the titanium plant should first use all of the chlorine gas that it generates rather than dispose of any. According to the Petitioners, the magnesium plant profits from this arrangement by receiving a higher credit for the gas generated. The Petitioners argue that accounting for the chlorine cycle at the titanium and magnesium plants in this manner creates a clear and unwarranted internal subsidy from the titanium mill to the magnesium mill. Accordingly, the Petitioners assert, the Department should recognize that the only surplus chlorine generated is at the magnesium mill. Thus, the Petitioners argue, the Department must reject Avisma's artificial and distortive methodology and recalculate the reported by-product offset

accordingly.

The Petitioners argue that the physical flow with regard to the chlorine gas offset can be restated by increasing the quantity of chlorine gas recycled at the titanium plant to equal the full quantity generated. The Petitioners assert that, as a consequence, the quantity of chlorine gas flowing from the magnesium plant to the titanium plant is reduced with a corresponding reduction in the by-product revenue generated at the magnesium plant. The Petitioners contend that this loss in by-product revenue at the magnesium plant must be treated as an increase in the unit cost of all magnesium products produced by Avisma during the POI.

Avisma argues that no adjustment is required with respect to chlorine gas. According to Avisma, the reported by-product offset for chlorine gas should remain unchanged because it is based on actual verified information. Avisma asserts that its chlorine data is used in the normal course of business and does not distort the dumping analysis. Avisma contends that if this actual data is not used, the cost of magnesium will be overstated because the Petitioners' allocation incorrectly assumes that there is no disposal of chlorine gas at the titanium workshop. Avisma points out that the record evidence shows that Avisma does in fact dispose of some chlorine gas at the titanium facility. Further, Avisma asserts, this evidence is based on daily production reports and actual amounts.

Avisma argues that even if any type of allocation is appropriate, it would be more appropriate to allocate chlorine gas based on the percentage of the total gas generated in the magnesium and titanium production facilities. Avisma maintains that this methodology would recognize the fact that some of the gas from the titanium facility is burned off. Accordingly, Avisma asserts, the amount of burned-off gas assumed to come from titanium production would be based on the percentage of gas produced at the titanium facility.

Department's Position:

We agree with the Petitioners that we should recalculate Avisma's reported offset for chlorine gas. Avisma generates chlorine gas as a by-product of both its magnesium and titanium production processes. During the POI, the magnesium workshop produced more chlorine gas than it was able to consume, and the titanium workshop consumed more chlorine gas than it was able to produce. Overall, Avisma disposed of significant quantities of chlorine gas. In the company's cost accounting records, these disposal quantities were distributed between both workshops. Thus, even though the titanium workshop was not able to generate enough gas to meet its chlorine gas consumption requirements, it still received credit for a significant quantity of disposals.

We do not dispute the fact that Avisma's treatment of the chlorine gas disposal quantities is based on verified information in its cost accounting and production records. We believe, however, that the information recorded in these records does not reflect the physical reality of Avisma's chlorine gas flows. Chlorine gas generated in both magnesium and titanium production is similar, and can be used interchangeably in either process. Additionally, all gas that is to be disposed of is sent to one central

location to be burned off. Thus, the decision as to which gas should be disposed of (i.e., the gas generated in the magnesium workshop or the gas generated in the titanium workshop) appears to be an arbitrary one, completely at the discretion of the company. Avisma could just as well have transferred all of the excess chlorine gas generated at the magnesium workshop to the titanium workshop first before burning it off, and recorded all disposals in its production records as having occurred at the titanium workshop.

Because the company can control which workshop's chlorine gas production to dispose of versus which to consume, we find it appropriate to determine the chlorine gas offset based on an analysis of each workshop's total gas generation in relation to its total gas consumption. Consequently, we do not find it reasonable to attribute any disposal quantities to the titanium workshop when the titanium workshop cannot even generate enough gas to meet its production needs. Because the total disposal quantity is more properly attributed to the only workshop that generates a surplus of chlorine gas, we have therefore attributed the total chlorine gas disposal quantity to the magnesium workshop and recalculated Avisma's chlorine gas offset accordingly.

Comment 9: Depreciation Expense

The Petitioners argue that the Department should adjust Avisma's reported depreciation costs to reflect significant inflation during the period from 1998 through 2003. According to the Petitioners, Avisma's asset values, as booked, significantly understate current asset values. The Petitioners contend that a review of the inflation rates experienced by Russia since Avisma last revalued its fixed asset base in 1997 make it clear that the purchasing power of the ruble has declined significantly. Thus, the Petitioners reason, the unadjusted ruble values of assets reported in Avisma's books significantly understate the actual value in 2003 rubles. The Petitioners maintain that because the depreciation in Avisma's financial records is based on these unadjusted values, the reported depreciation expense is likewise significantly understated.

The Petitioners argue that the 2001 appraisal study submitted by Avisma, in exhibit 7 of its September 9, 2004 Supplemental Section D Questionnaire Response, also shows that Avisma's asset values, as booked, fail to reflect current asset values. The Petitioners assert that a review of the data in the 2001 appraisal shows that the asset values booked by Avisma are only a fraction of the actual values.

The Petitioners argue that although Avisma's decision not to revalue its fixed assets is permissible under Russian GAAP, the Department should still adjust the reported depreciation expense to avoid distortions to the antidumping analysis. The Petitioners maintain that under section 773(f)(1)(A) of the Act, if a company's normal books and records kept in accordance with local GAAP do not reasonably reflect the actual costs associated with the production and sale of merchandise, it is the Department's practice to reject those records. See, e.g., Micron Tech., Inc. v. United States, 893 F. Supp. 21, 34 (CIT 1995) and Notice of Final Determination of Sales at Less Than Fair Value: Certain Hot-Rolled Carbon Steel Flat Products from India, 66 FR 50406 (October 3, 2001) and accompanying Issues and Decision Memorandum, at Comment 12. Thus, the Petitioners contend, an adjustment to Avisma's

depreciation expense would be in accordance with the statute and the Department's long-standing practice.

The Petitioners argue that the Department should recalculate the reported cost of production (COP) data to capture the amount by which Avisma's reported depreciation expenses are understated. Specifically, the Petitioners assert, the Department should adjust the historical fixed asset values to reflect current values by determining the ratio of inflation-adjusted fixed asset values to unadjusted historical fixed asset values and applying this ratio to the reported depreciation expenses. The Petitioners suggest that the Department should calculate the current asset values using the fair-market value data contained in Avisma's 2001 appraisal report. In the alternative, the Petitioners add, if the Department decides not to rely on this data, it can calculate the adjusted fixed asset values based on the inflation rates in Russia (*i.e.*, the producer price index as reported by the International Monetary Fund in International Financial Statistics (May 2004)) during the years since the last revaluation (*i.e.*, the period from 1998 to 2003). In either case, the Petitioners assert, the Department has verified data with which to restate Avisma's fixed asset values and determine the amount by which the recorded book values are understated.

Avisma argues that the Department should not adjust its reported depreciation expenses. According to Avisma, Russia was not experiencing high inflation during the POI and the Department does not normally go back to prior periods to revalue assets. Avisma cites Notice of Final Determination of Sales at Less Than Fair Value: Cut-to-Length Carbon Steel Plate Products from Indonesia, 64 FR 73164, 73170 (December 29, 1999), and asserts that the Department's normal rule for considering whether to adjust for inflation is whether the country of manufacture experienced 25 percent or greater inflation during the period of investigation or review. In the current investigation, Avisma points out, the inflation rate in Russia during the POI was 15.49 percent, well below the 25 percent threshold (See Avisma Cost Verification Report at page 4²⁷). Avisma acknowledges that in a number of cases, the Department has adjusted a respondent's depreciation for inflation that was significant but not hyper-inflationary, but asserts that it does not know of any case where the adjustment was based on inflation experienced during periods prior to the period of investigation or review.

Avisma argues that the Department cannot adjust its recorded depreciation based on prices that occurred during the non-market period. Avisma argues that the Department made clear in the Graduation Memorandum, that the Department never intended to review transactions on a market economy basis until after the effective graduation date in April 2002. Furthermore, Avisma asserts, the Department has stated in numerous cases that for purposes of the dumping calculation, it would not rely on prices in a NME. Avisma contends that adjusting its 2003 depreciation based on data prior to April 2002 is improper because it would be using NME prices as a benchmark for market-economy prices. Avisma reasons that inflation figures are based on prices and, thus, the inflation figures prior to April 2002 cannot be relied upon for determining an antidumping margin.

²⁷ Memorandum to Neal M. Halper from Robert Greger, et al, Verification Report on the Cost of Production and Constructed Value Data Submitted by JSC AVISMA Titanium-Magnesium Works December 30, 2004 (Avisma Cost Verification Report).

Avisma maintains that its reported depreciation expense is consistent with Russian GAAP and should be used for purposes of calculating COP. Avisma cites Certain Steel Concrete Reinforcing Bars from Turkey; Final Results of Antidumping Duty Administrative Review, 66 FR 56274 (November 7, 2001) and accompanying Issues and Decision Memorandum, at Comment 16, and asserts that in accordance with section 773(f)(1)(A) of the Act, the Department's long-standing practice is to rely on the data in a respondent's normal books and records where those records are prepared in accordance with home country GAAP and reasonably reflect the COP. Accordingly, Avisma asserts, it is the Department's practice to rely on the depreciation expense recorded in the reporting company's financial statements. See Notice of Final Determination of Sales at Less Than Fair Value: Stainless Steel Bar from Italy, 67 FR 3155 (January 23, 2002) and accompanying Issues and Decision Memorandum, at Comment 48. Moreover, Avisma notes, section 773(f)(1)(A) also states that the Department will consider whether allocations have been historically used by the exporter or producer. Finally, Avisma asserts, the SAA at 834 states that an exporter or producer is expected to demonstrate that it has historically used its allocation methodologies particularly with regard to the establishment of appropriate amortization and depreciation periods. Avisma points out that its decision not to revalue its assets is both consistent with Russian GAAP and consistent with its past practice.

Avisma argues that its decision to not revalue its fixed assets is also consistent with U.S. GAAP. According to Avisma, the SAA, at 834, explains that the Department will consider U.S. GAAP in determining whether a company's records reasonably reflect costs. Under U.S. GAAP, Avisma argues, it is clear that plant and machinery should not be written up above acquisition cost even to reflect appraisal value as would be the case here (see APB Opinion No. 6, Status of Accounting Research Bulletins, paragraph 17). Therefore, Avisma reasons, even if the appraisal value exceeds book value, Avisma's depreciation should not be adjusted consistent with U.S. GAAP.

Avisma argues that the adjustment methodologies proposed by the Petitioners have significant flaws and would overstate depreciation expense. Avisma contends that the data in the 2001 appraisal report is flawed because both the replacement values and fair-market values in the report are based on NME prices. Further, Avisma asserts, using the study would grossly overstate any adjustment because it fails to recognize acquisitions and disposals that occurred from 1998 to 2003. According to Avisma, the Producer Price Index (PPI) data referred to by the Petitioners suffers from some of the same flaws as the data in the appraisal report as it relies wholly or partially on NME prices.

Avisma maintains that the appraisal report was done for insurance and financing purposes and was not intended for any other purpose. According to Avisma, the Petitioners have not cited one case where the Department has substituted values from an insurance appraisal for the recorded book value of assets. Moreover, Avisma argues, the appraisers also changed the average useful lives from those used by Avisma, which diminishes the comparability between values. Finally, Avisma asserts, the 2003 update to the 2001 study is also a flawed benchmark for these same reasons.

Department's Position:

We agree with the Petitioners that Avisma's depreciation expense should be adjusted. Under section

773(f)(1)(A) of the Act, costs are normally calculated based on the records of the exporter or producer if such records are kept in accordance with GAPP of the exporting or producing country and reasonably reflect the costs associated with the production and sale of the merchandise. Although the depreciation expense reported by Avisma was based on Avisma's accounting records prepared in accordance with Russian GAAP, it relies on fixed asset values from as far back as 1997. Moreover, we note that Russia experienced significant inflation during the subsequent period from 1998 up to the 2003 POI. Specifically, the change in the PPI was 7.03 percent, 58.95 percent, 46.53 percent, 19.17 percent, 11.55 percent and 15.49 percent in the years from 1998 through 2003, respectively (see International Financial Statistics, International Monetary Fund (May 2004)). Because a large part of Avisma's fixed asset values are recorded in 1997 rubles, they do not reflect the real value in current currency terms and are thus significantly understated. Accordingly, because the reported depreciation expense is based on these understated values, we do not find that it reasonably reflects Avisma's true current production costs.

With regard to Avisma's argument that the Department's rule for adjusting for inflation is whether the country experienced 25 percent or greater inflation during the POI or POR, we find this argument to be misplaced. This rule applies only to the decision regarding whether the Department should apply its high inflation methodology, and is not meant as a reasonableness test of whether a company's fixed assets are properly valued. Moreover, in cases involving countries whose economies, while not reaching the high inflation methodology threshold of 25 percent during the POI or POR, nonetheless are continually marked by high inflation from year to year, the Department has adjusted the respondent's depreciation expense for inflation in order to permit a more appropriate matching of costs and prices based on equivalent currency units. See, e.g., Certain Fresh Cut Flowers from Colombia: Final Results of Antidumping Administrative Reviews 61 FR 42833, 42844 (August 19, 1996). Thus, while the Russian economy did not meet the Department's high inflation standard during the POI, the significant inflation that occurred in the years from 1997 to 2003 must be accounted for in Avisma's fixed asset values when calculating depreciation expense for the POI.

Regarding Avisma's argument that its decision not to revalue its assets is consistent with U.S. GAAP, we note that U.S. GAAP does not provide for the revaluation of fixed assets because inflation in the U.S. economy is consistently low. Thus, in this instance, U.S. GAAP does not provide a suitable standard for judging the reasonableness of revaluing fixed assets in an economy that has experienced significant inflation.

In evaluating how to properly restate Avisma's fixed asset values and capture the resulting depreciation expense at current levels, we find that there are three alternative methodologies available on the record of this investigation: 1) adjust the fixed asset values to fair-market value using the 2001 appraisal report; 2) adjust the fixed asset values to fair-market value using the 2003 appraisal report; or 3) adjust the fixed asset values using the PPI data published by the International Monetary Fund (IMF). While all three options are reasonable, we believe that the record evidence shows that adjusting the fixed asset values using the 2003 appraisal report is preferable. The information in the 2003 appraisal is more contemporaneous with the POI and it reflects a certified measure of the current value of Avisma's fixed assets established during a market economy period. Further, the values in the appraisal are

measured at a specified point in time and thereby reflect all additions and disposals of fixed assets that occurred in prior periods. While both parties argue extensively about the appropriateness of using the 2001 appraisal report, because we are not using that report in our final determination, we will not address those points here. Therefore, for the final determination, we have adjusted Avisma's fixed asset values and resulting depreciation expense based on the information in the 2003 appraisal report.

Comment 10: Non-Operating Income and Expenses

The Petitioners argue that the Department should increase the G&A expense ratio to account for other operating and non-operating expenses excluded by Avisma. The Petitioners refer to the Avisma Cost Verification Report at page 3 and assert that other than foreign exchange gains and losses and certain prior period costs, all of these items relate to the general operations of the company. Thus, the Petitioners contend, the Department should include these items in G&A for the final determination.

Avisma argues that the Department should not adjust the G&A ratio for the excluded other operating and non-operating items. Avisma cites Notice of Final Determination of Sales at Less Than Fair Value: Certain Cut-To-Length Carbon-Quality Steel Plate Products from Korea, 64 FR 73196, 73209 (December 29, 1999), and asserts that in analyzing whether to include an item in G&A, the Department considers the nature of the activity and whether the activity is significant enough to be treated separately from the respondent's other business activities. According to Avisma, a review of the other operating and non-operating items clearly shows that numerous expenses are not related to the general operations of the company. In the alternative, if the Department makes such an adjustment, Avisma maintains that the foreign exchange gains and losses and any amounts related to a certain affiliated party loan should not be included in the revised G&A figure.

Department's Position:

We agree with the Petitioners that Avisma's G&A ratio should be adjusted. The Department's established practice is to include in the G&A ratio calculation all revenues and expenses that relate to the general operations of the company as a whole. See, e.g., Silicomanganese from Brazil: Final Results of Antidumping Administrative Review 69 FR 13813 (March 24, 2004) and accompanying Issues and Decision Memorandum, at Comment 10 (Silicomanganese from Brazil); Notice of Final Determination of Sales at Less Than Fair Value: Certain Cold-Rolled Carbon-Steel Flat Products from Taiwan, 67 FR 62104 (October 3, 2002) and accompanying Issues and Decision Memorandum, at Comment 6; and Notice of Final Determination of Sales at Less Than Fair Value: Certain Cold-Rolled Flat-Rolled Carbon-Quality Steel Products from Taiwan, 65 FR 34658 (May 31, 2000) and accompanying Issues and Decision Memorandum, at Comment 11. Accordingly, in determining whether particular items should be included in G&A, the Department reviews the nature of the item and its relation to general operations. At verification, the Department performed a detailed review of the other operating and non-operating revenues and expenses in Avisma's financial statements and noted that these items include gains and losses from the sales of fixed assets, penalties, fines, service charges, subscriptions and other miscellaneous expenses. None of these items was so significant as to constitute a separate line of business. With the exception of foreign exchange gains and losses and certain prior

period costs, all of the items in question relate to general operations. Therefore, we have included these items in the G&A ratio calculation for the final determination.

Comment 11: Interest on Affiliated Party Loan

The Petitioners argue that the Department should recalculate Avisma's financial expense ratio to reflect interest expenses related to an affiliated party loan. The Petitioners contend that the Department should reject Avisma's exclusion of all interest expenses related to this loan from the 2003 total financial expenses. According to the Petitioners, Avisma's treatment of these interest expenses inappropriately excludes a major expense incurred by Avisma from the ratio calculation and results in a distortion in the reported COP.

The Petitioners assert that Avisma did not provide support for its claim that Russian GAAP required the company to capitalize the interest related to this loan because of the specific use of the proceeds. The Petitioners contend that while capitalization of the interest expense may be in accordance with Russian GAAP, it may not be the only option. According to the Petitioners, Avisma may well have been able to expense the interest in the current year. Moreover, the Petitioners argue, whether the interest expense is booked to the profit and loss statement or the balance sheet, it is still a real, current cost to Avisma.

The Petitioners assert that U.S. GAAP allows for the capitalization of interest only in cases where the associated loans are used to acquire certain types of assets. The Petitioners refer to Statement of Financial Accounting Standards (SFAS) No. 34 and point out that to qualify for interest capitalization under U.S. GAAP, assets must require a period of time to prepare them for their intended use. Further, the Petitioners note, under SFAS No. 58, the capitalization of interest expense related to investments is allowed only prior to the commencement of operations of the investee. The Petitioners contend that Avisma's use of this loan does not in any way meet the standard under U.S. GAAP.

The Petitioners argue that the loan extended to Avisma by its affiliate was not made at arm's length and does not reflect market conditions. The Petitioners assert that, because the transaction is between two affiliated parties, the Department is obligated to examine whether or not the loan is an arm's-length transaction. According to the Petitioners, the 2003 interest rate on the affiliated party loan stands in stark contrast to the initially agreed-upon rate. Further, the Petitioners contend, a comparison to standard market data on interest rates in Russia during 2003 indicates that the rate charged to Avisma is not reflective of market conditions (see International Financial Statistics (May 2004)). Accordingly, the Petitioners argue, the Department should reject Avisma's exclusion of the interest expense on the loan from its affiliate and apply its standard arm's-length criteria to the loan in order to calculate an interest expense based on the higher of the transfer price, the market price, or the cost of the loan. See, e.g., Notice of Final Determination of Sales at Less Than Fair Value: Silicomanganese from Venezuela, 67 FR 15533 (April 2, 2002) and accompanying Issues and Decision Memorandum, at Comment 3. The Petitioners contend that based on this arm's-length test, the Department should calculate the interest expense on this loan based on the rate in the original loan agreement.

Avisma argues that the Department should not adjust its financial expense ratio to include interest

expense on its affiliated party loan. Avisma contends that the expense should not be included in the financial expense ratio because it was not related to production. Moreover, Avisma maintains, because the interest on this loan was clearly tied to investment activity, it should not be included in Avisma's costs. Avisma cites Notice of Final Determination of Sales at Less Than Fair Value: Fresh Atlantic Salmon from Chile, 63 FR 31411, 31436 (June 9, 1998) and Circular Welded Non-Alloy Steel Pipe from the Republic of Korea: Final Results of Antidumping Administrative Review 66 FR 18747 (April 11, 2001) and accompanying Issues and Decision Memorandum, at Comment 11, and asserts that it is the Department's position that expenses related to investment activities should not be included in a respondent's costs.

Avisma argues that the Department verified that the treatment of the interest expense on its affiliated party loan was consistent with Russian GAAP. Furthermore, Avisma asserts, whether or not U.S. GAAP allows for the capitalization of interest, it is not the final word on the treatment of non-operating expenses in antidumping cases. Therefore, Avisma concludes, in accordance with past practice, the Department should not include the interest expense on the affiliated party loan in Avisma's financial expense ratio.

Department's Position:

We agree with Avisma that we should not include the interest on its affiliated party loan in the calculation of the financial expense ratio, albeit not for the same reasons cited by Avisma. Due to the proprietary nature of the specific information involved, however, a meaningful discussion of our position on this issue is not possible in this public memorandum. We have therefore addressed our position in a separate memorandum which will be placed on the official record. See Memorandum to Neal M. Halper from Robert B. Greger, Re: Cost of Production and Constructed Value Calculation Adjustments for the Final Determination, February 16, 2005.

Comment 12: Foreign Exchange Gains and Losses

The Petitioners argue that the Department should continue to increase the financial expense ratio to reflect foreign exchange losses as it did at the preliminary determination. The Petitioners assert that the Department correctly concluded in its Preliminary Determination that these losses should have been reported as part of the financial expense factor. Thus, the Petitioners conclude, the Department should include the net foreign exchange losses in the ratio calculation in the final determination.

Department's Position:

We agree with the Petitioners that the financial expense ratio should reflect foreign exchange losses. Our practice is to include in the financial expense ratio calculation the total net foreign exchange gain or loss reported in the financial statement of the same entity used to compute a respondent's net interest

expense. See, e.g., Silicomanganese from Brazil and accompanying Issues and Decision Memorandum, at Comment 14; Stainless Steel Bar from India: Final Results of Antidumping Duty Administrative Review, 68 FR 47543 (August 11, 2003); and accompanying Issues and Decision Memorandum, at Comment 6, and Certain Preserved Mushrooms from Indonesia: Preliminary Results of Antidumping Duty Administrative Review and Intent to Revoke Order in Part, 68 FR 11051 (March 7, 2003). Thus, for purposes of this final determination, we have continued to include the total net foreign exchange losses from Avisma's 2003 financial statements in the financial expense ratio calculation.

Comment 13: Model Matching of Certain SMW Products

SMW argues that the model matching criteria used in the Preliminary Determination lead to erroneous matching of two of SMW's products, a secondary alloy product made from scrap and sold in the United States and a special-grade product made from 100 percent primary magnesium sold in the home market. SMW claims that these two products are sold at very different prices and are composed of different source materials. SMW suggests that, because there is no comparable product in the home market, the Department should use constructed value (CV) to calculate normal value for this secondary alloy product.

Department's Position:

Like Avisma, SMW did not raise any concerns with the Department's model match criteria until verification. Even at this point, SMW does not suggest how the model matching criteria should be altered, but instead recommends that for sales of secondary alloys to the United States the Department move directly to CV.

However, as the Federal Circuit has held, "{t}he plain language of the statute requires Commerce to base foreign market value on nonidentical but similar merchandise . . . rather than CV when sales of identical merchandise have been found to be outside the ordinary course of trade." Cemex, S.A., v. United States, 133 F.3d 897, 904 (Fed. Cir., Jan. 8, 1998). Therefore, as long as sales of similar home-market products are available (i.e., above cost, within the "difmer" test for similarity, and otherwise within the ordinary course of trade) the Department must use those sales for price-to-price comparisons before resorting to CV.

Comment 14: Date of Sale

SMW argues that the Department, in its final determination, should adopt contract date as the date of sale for its U.S. sales. SMW claims that most of its U.S. sales are made pursuant to long-term or annual contracts. SMW argues that the Department should use contract date because this is when the terms of the sale (i.e., price and quantity) are established, or, in the event of a contract amendment, re-established. SMW notes that the Department reviewed the various types of contracts issued by both U.S. affiliates during verification, including those contracts that provided for price and quantity renegotiation.

SMW also argues that contract date is the appropriate date of sale because the Department used contract date in a previous investigation of magnesium from Russia in 2000-2001. In the course of that investigation, the Department even instructed SMW to report post-POI shipments made pursuant to contracts concluded or amended during the POI. SMW claims that the type of long-term contracts and the conditions of sale in the current investigation are the same as they were in the previous case.

The Petitioners argue that the Department should continue to use invoice date as date of sale for SMW's U.S. sales. The Petitioners claim that the Department's regulations create a presumption that invoice date is the date of sale unless it is demonstrated to the Department's satisfaction that the material terms of sale cannot change prior to invoicing. They assert that SMW has not demonstrated that it is entitled to an exception to the Department's normal practice of using invoice date as the date of sale. According to the Petitioners, what SMW's affiliates are characterizing as "contracts" are, in fact, non-binding supply agreements. The Petitioners cite facts within the verification reports demonstrating that many customers continue to submit purchase orders to the U.S. affiliates even though contracts are supposedly in place.

Department's Position:

According to section 351.401(i) of the Department's regulations, in identifying the date of sale the Department "normally will use the date of invoice . . . However, the Department may use a date other than the date of invoice if the {Department} is satisfied that a different date better reflects the date on which the exporter or producer establishes the material terms of sale."

The Department has determined that SMW has not brought to our attention sufficient information to demonstrate that the Department should depart from its presumptive date of sale, the invoice date. See SeAH Steel Corp. V. United States, Ct. No. 00-04-00157, slip op. 01-20 at 6, n.1 (CIT February 23, 2001). SMW makes all its U.S. sales through two affiliated importers, Solimin and Cometals. While the Department verified that Cometals in general ships and invoices its sales according to the terms of its contracts, the Department also saw at verification that Solimin often does not. When examining long-term contracts, we saw that "{i}f the price is renegotiated, according to Solimin, an amended contract is not always issued. Regardless of these long-term contracts, quantities and shipment schedules are also flexible." See page 5 of Solimin Verification Report.²⁸ Thus, revisions to contracts are not always memorialized and amended contract dates do not always exist. Moreover, it is problematic to use contract dates, or amended contract dates, if it is not unusual for the underlying contract terms to be revised freely, especially if such revisions are the result of changing market conditions. The terms of such contracts cannot be said to be fixed, if both parties know that the terms may change as circumstances dictate.

²⁸ Memorandum to the File, from Joshua Reitze and Kimberley Hunt, Magnesium Metal From The Russian Federation: Magnesium Metal From The Russian Federation: U.S. Sales Verification, December 29, 2004 (Solimin Verification Report).

The Department described just this type of situation in the preamble to the regulation addressing date of sale:

The existence of an enforceable sales agreement between the buyer and seller does not alter the fact that, as a practical matter, customers frequently change their minds and sellers are responsive to those changes. The Department also has found that in many industries, even though a buyer and seller may initially agree on the terms of sale, those terms remain negotiable and are not finally established until the sale is invoiced. . . . A preliminary agreement on terms, even if reduced to writing, in an industry where renegotiation is common does not provide any reliable indication that the terms are truly “established” in the minds of the buyer and seller.

Antidumping Duties; Countervailing Duties; Final Rule, 62 FR 27296, 27348-49 (May 19, 1997).

Furthermore, while the terms of most of Cometals’ contracts examined by the Department at verification were fulfilled without change, one was not. While such a record might be enough to conclude that Cometals’ contracts “generally are adhered to,” it does not support the conclusion that contract date is more reliable than invoice date for purposes of our methodology, especially when viewed in combination with the sales practices of SMW’s shipments through Solomin. See Cometals Verification Report.²⁹ As noted above, our regulations require the use of invoice date unless another date is found that “better” reflects when the terms of sale are fixed.

Finally, we agree with the Petitioners that SeAH, Slip Op. 01-20 (CIT Feb. 23, 2001), is on point here. In that case, SeAH Steel Corp. argued that contract date was the appropriate date of sale, even when the terms of the contract changed, because those changes could be characterized as “amended contracts.” In response, the CIT stated:

Notwithstanding plaintiff’s attempt to characterize the faxed changes as simply an “amendment to the contract,” . . . and therefore not a change warranting use of invoice date as the date of sale, such postcontract modifications are precisely the sort of “amendments” that form the basis of the Department’s regulatory presumption in favor of invoice date.

Id. at 9.

Comment 15: Sales to the Russian Government Stockpile

SMW argues that sales made to the Russian government stockpile should be disregarded for the final

²⁹ Memorandum to the File, from Joshua Reitze and Kimberley Hunt, Magnesium Metal From The Russian Federation: Magnesium Metal From The Russian Federation: U.S. Sales Verification (Cometals), December 30, 2004 (Cometals Verification Report).

determination because they are outside the ordinary course of trade, as defined in 19 U.S.C. 1677 (15). SMW notes that stockpile sales differ from sales of the same product made by SMW in the ordinary course of trade because: (1) they are made to the government, which is a non-commercial entity, and the product is used for non-commercial purposes; (2) the Russian government can legally compel SMW to supply the stockpile; (3) the contract specifies unique packing requirements absent in other sales of the same material; (4) the contract requires SMW to provide a ten-year guarantee on this material (as opposed to six months on non-stockpile sales); and (5) the price on these sales is different than the price of non-stockpile sales of the same product.

The Petitioners contend that these sales should be included in the Department's final determination. They argue that sales to the government stockpile are not outside the ordinary course of trade. The Petitioners claim that such a determination must be based on all pertinent factors, not simply factors that have been selectively chosen by respondents, such as sales terms and price. The Petitioners claim that the totality of the evidence demonstrates that the stockpile sales were made in the ordinary course of trade. The Petitioners further note that the record indicates that the stockpile contract was negotiated by both parties under normal business terms and under normal commercial circumstances.

Department's Position:

The Department has determined that SMW's sales to the Russian government stockpile are not outside the ordinary course of trade and should be used in calculating normal value. We agree with SMW's claim that the Department should examine such factors as "quantity, pricing, sales terms, and customer type" in making this determination, and that ultimately such a determination should be based on "the totality of the circumstances." However, we conclude that an examination of all the factors cited by SMW and the Petitioners does not lead to a conclusion that these sales are outside the ordinary course of trade. In particular, we find that:

1. Stockpile sales constitute a significant portion of SMW's home-market sales.
2. The products sold to the stockpile do not differ in physical characteristics from products commonly sold to other customers; in fact, they are identical. They differ only in terms of packaging, and the guarantee provided by SMW is reflected only in a promise to replace defective merchandise, not in different physical qualities.
3. SMW's argument regarding the price of stockpile sales involves solely a discussion of gross price. SMW does not provide any argument that the adjusted net price of the product differs from that of identical merchandise sold to other customers. The failure to demonstrate the anomalous nature of the net price of these sales is especially important in this case, given that differences noted by SMW, *e.g.*, packing and guarantee expenses, would be adjusted for by the Department prior to any comparison to U.S. sales.
4. SMW does not reference any factual information on the record to support its conclusion that this stockpile magnesium is not used for consumption. While undoubtedly the material is being purchased to be held in storage for the immediate future, clearly the purpose of the purchase is

to ensure adequate supply of magnesium at a time in the future, when demand may exceed the supply available in the market. We believe that the relevant distinction between commercial and non-commercial customers refers not to present versus future consumption (in manufacturing or otherwise), but to customers who intend to consume or resell the product versus customers who buy samples purely for evaluation purposes. See, e.g., Granular Polytetrafluoroethylene Resin from Japan: Final Results of Antidumping Duty Administrative Review, 58 FR 50343, 50345 (Sept. 1993) (“{T}he sales in question are also not for consumption, but rather for evaluation purposes . . .”).

5. There is no Department precedent for concluding that sales to governments are outside the ordinary course of trade per se or in combination with other facts. In fact, in another case we rejected a claim that sales to government agencies should be considered outside the ordinary course of trade because they were supposedly “state controlled” and not made under “free market” conditions. See Final Determination of Sales at Less than Fair Value; Generic Cephalexin Capsules from Canada, 54 FR 26820 (June 26, 1989).

SMW cites a Russian law which allows the Russian government to compel certain manufacturers to conclude contracts to supply materials to state stockpiles. While SMW brought this law to the Department’s attention at verification, SMW also stated that “there is some amount of negotiation involved regarding the price” and made two additional claims, which are business-proprietary, suggesting that while SMW might be compelled to conclude these contracts, it is not compelled to accept precise terms of sale. See SMW Verification Report³⁰ at 9. Moreover, there is no evidence on the record which supports the conclusion that SMW was in fact forced to enter into the transactions at issue. The Department also learned at verification that Avisma had in past years sold magnesium to the government stockpile, but did not make any such sales during the POI. In addition to supporting the conclusion that these sales are not unordinary, the fact that Avisma did not make such sales during the POI indicates they may not be as compulsory as SMW suggests. See Avisma Verification Report at 21.

Comment 16: Certain Selling Expenses on Sales to the Stockpile

The Petitioners claim that home-market indirect selling expenses improperly include an amount for certain alleged expenses related to sales to the government stockpile. The Petitioners argue that these expenses should not be included in the calculation of home-market indirect selling expenses because they constitute a direct selling expense. Moreover, the Department rejected information related to these expenses at verification for being untimely new factual information and did not verify any facts concerning these expenses.

SMW agrees with the Petitioners that the expenses in question are not indirect selling expenses. SMW explains that, at verification, they were used in the reconciliation of SMW’s total selling expenses in

³⁰ Memorandum to the File, from Maria MacKay and Mark Hoadley, Magnesium Metal From The Russian Federation: Verification Report for Solikamsk Magnesium Works, December 27, 2004 (SMW Verification Report).

SMW's financials (which do not include these expenses) to the total selling expenses recorded in SMW's management reports (which do include these expenses), as described in the verification report.

Department's Position:

As noted in our report, the Department determined at the sales verification that the indirect selling expenses reported in the sales database were incorrect. We were able, however, to verify the indirect selling expenses reported in the cost database and matched them to the management reports in which selling expenses are recorded on a product-specific basis. Because the expenses in question were not included in indirect selling expenses for the product in question in the cost database, these expenses are not factored into the indirect selling expense calculation. Hence, no adjustment is necessary.

Comment 17: Domestic Inventory Carrying Costs

The Petitioners urge the Department to include in the calculation of inventory carrying costs for U.S. sales a value for days in inventory at SMW. This would correct an omission by SMW explained in the Department's verification report.

SMW notes that the Department did verify the average time during which subject merchandise was held in inventory at the plant. SMW argues that the calculations were based on an average of two alternate inventory periods, and that this average was verified and confirmed as accurate by the Department.

Department's Position:

As we noted in the verification report, SMW's domestic inventory carrying cost for its U.S. sales includes days at sea, but not days in inventory at SMW's Russian facilities. See SMW Verification Report at 17. Therefore, for the final determination, we will increase domestic inventory carrying costs by the number of days held at SMW's Russian facilities.

Comment 18: Selling Expenses Reported in the Cost File

SMW claims that it inadvertently included selling expenses in the reported COP. SMW maintains that the same selling expenses were included in both the variable overhead field of the cost file, and in SMW's Sections B and C questionnaire response. SMW argues that for the final determination, the Department should remove selling expenses from the reported cost.

The Petitioners point out that, while SMW included selling expenses in the reported COP, the company failed to suggest a method for the Department to correct this error. According to the Petitioners, the impact of the error on the reported cost can be determined by expressing the amount of incorrectly included selling expenses as a percentage of the total cost of manufacturing (COM), and then reducing the reported COM of each control number (CONNUM) by that ratio.

Department's Position:

We agree with the Respondent that certain selling expenses were inadvertently included in the reported COP. At verification, we noted that product-specific selling expenses were reported for each sale in the home-market and U.S. sales databases, and the same per-unit expenses were also reported in the cost file. We disagree with the Petitioners that this adjustment should be expressed as a ratio of the total selling expenses to the total COM. We note that SMW reported selling expenses as a separate data field in the cost database (i.e., field VOH2, see SMW Cost Verification Report³¹ at Exhibit 9). Accordingly, for the final determination, we have adjusted the reported cost to exclude this field (i.e., field VOH2) from the cost database.

Comment 19: General and Administrative (G&A) Expenses

SMW notes that during the cost verification, the Department identified a number of income and expense items that were excluded from the reported costs. The Respondent argues that if the Department decides to adjust the reported G&A expense rate for these items, certain expenses should be disregarded for the purposes of the adjustment. The Petitioners argue that all of these items should be included in the G&A expense.

We cannot meaningfully summarize or address the specifics of the Respondent's and the Petitioners' arguments regarding this issue in this public memorandum, as a thorough discussion is only possible by means of reference to business proprietary information. We have addressed the parties' arguments, as well as our position, in a separate memorandum which will be placed on the official record. See Memorandum from Ernest Gziryan to Neal Halper regarding Cost of Production and Constructed Value Calculation Adjustments for the Final Determination, dated February 16, 2005. A public version of this memorandum is on file in the Department's CRU.

Comment 20: Factory Overhead

SMW argues that the reported factory overhead cost was properly based on the company's internal management reports. The Respondent concedes that the total amount of the factory overhead recorded in the audited financial statements differs from the amount of factory overhead in the management reports. SMW claims that the difference is attributable to the cost of products produced specifically for the Russian stockpile. Thus, according to the Respondent, any adjustment to factory overhead should be made only to the cost of products for the stockpile, and because sales to the stockpile are outside the ordinary course of trade, no adjustment to the factory overhead cost is required. The Respondent further suggests that if the stockpile sales are not excluded from consideration, the Department should allocate the additional overhead costs based on quantities

³¹ Memorandum to Neal M. Halper from Ernest Gziryan, et al; Verification Report on the Cost of Production and Constructed Value Data Submitted by Solikamsk Magnesium Works, December 30, 2004 (SMW Cost Verification Report).

shipped over the years in which sales to the Russian stockpile were made (i.e., 2003 and 2004).

The Petitioners argue that, while it may be correct that the expenses at issue are specifically attributable to the stockpile sales, the fact remains that all costs related to the production of the subject merchandise should be reflected in the reported costs. The Petitioners note that because the Department requires respondents to report a single weighted-average cost per CONNUM based on production volume regardless of market, the nature of specific sales of that product does not enter into consideration. Accordingly, the Petitioners conclude, the Department should adjust SMW's fixed overhead cost to account for the unreported difference.

Department's Position:

We agree with the Petitioners that all costs related to the production of the subject merchandise during the POI should be included in the reported COP. The fact that some products manufactured during the POI were later sold as stockpile material should have no effect on the reported COP for these products. Thus, the additional factory overhead costs should be included in the costs for the relevant CONNUM.

Regarding the Respondent's argument that because the additional expenses are attributable only to the cost of stockpile products, and because sales to the stockpile are outside the ordinary course of trade, no adjustment to factory overhead cost is required, we disagree. First, we note that we have determined to include stockpile sales as we have not found that they are outside the ordinary course of trade. Second, we note that the expenses at issue were recorded in SMW's audited financial statements as factory overhead, which normally includes expenses not directly attributable to specific sales of products. Moreover, in calculating a single weighted-average cost for each CONNUM, the worldwide production quantities of all products with similar matching characteristics should be included. Record evidence shows that the stockpile sales fall within the same CONNUM as other non-stockpile products based on the Department's matching characteristics. Thus, the cost of these products should be included in the reported CONNUM-specific costs. Accordingly, for the final determination, we have increased the reported fixed overhead cost to reflect the total amount of fixed overhead as recorded in SMW's audited financial statements.

Comment 21: By-product Offset

SMW claims that it properly valued by-product chlorine gas generated during the POI. The Petitioners argue that the Department should reject SMW's claim for a by-product offset for chlorine gas generated by the magnesium production unit and transferred to other production units.

We cannot meaningfully summarize or address the specifics of the Respondent's and the Petitioners' arguments regarding this issue in this public memorandum, as a complete discussion is only possible by means of reference to business proprietary information. We have addressed the parties' arguments and our position in a separate memorandum which will be placed on the official record. See Memorandum

from Ernest Gziryan to Neal Halper regarding Cost of Production and Constructed Value Calculation Adjustments for the Final Determination, dated February 16, 2005. A public version is on file in the Department's CRU.

Comment 22: Major Input

SMW purchased carnallite, which is used in magnesium production, from an affiliated company. Because carnallite constitutes a major input in the production of magnesium, the Petitioners suggest that the Department should adjust SMW's reported cost of manufacturing to reflect the higher of the transfer price, market price, or COP of carnallite in accordance with section 773(f)(3) of the Act.

SMW argues that if the Department decides to make an adjustment to SMW's cost of manufacturing as proposed by the Petitioners, it should use for comparison the cost of carnallite as recorded in SMW's books rather than the average transfer price paid to an affiliated supplier.

Department's Position:

We agree with the Petitioners that the application of the major input rule in accordance with section 773(f)(3) of the Act is warranted in this case. For the final determination, we adjusted the reported cost of carnallite purchased from an affiliated supplier in accordance with the major input rule of section 773(f)(3). As to the Respondent's argument that the cost as recorded in SMW's books should be used for comparison, we note that the cost of carnallite recorded in SMW's books includes, in addition to the transfer price paid to an affiliated supplier, the cost of certain services provided by unaffiliated companies. We note that, while SMW included the cost of these services in the cost of carnallite, the services are provided by an unaffiliated company after the carnallite is purchased. Thus, we find that the cost of these services is not part of the transfer price paid to the affiliated supplier, and we excluded these costs from our analysis.

Comment 23: Weighted Average Per-Unit Cost

The Petitioners note that in the reported cost database, SMW provided multiple costs for the same CONNUM. The Petitioners argue that the Department should revise the reported cost for this CONNUM to reflect a single weighted-average cost. The Petitioners further claim that because SMW did not provide the production quantity for the product with the highest per-unit cost included in this CONNUM, it is not possible for the Department to accurately calculate a weighted-average cost. As such, the Petitioners conclude, the Department should base the cost for this CONNUM strictly on the cost of that specific product.

The Respondent refutes the Petitioners' claim that SMW did not provide the production quantity for one of the products included the CONNUM at issue. SMW points out that SMW provided production quantity for this product in its response to Section D of the Department's questionnaire, as well as at verification. Thus, according to SMW, a weighted-average cost for this CONNUM can

easily be calculated. SMW further argues that because one of the products included in this CONNUM represents product sold to the Russian stockpile, and because sales to the stockpile were made outside the ordinary course of trade, the cost of this product should not be included in the calculation of the weighted-average cost for this CONNUM.

Department's Position:

We agree with both parties that a single weighted-average cost must be calculated for each CONNUM. We note that, contrary to the Petitioners' claim, SMW provided production quantity for all products included in the CONNUM at issue. See SMW's August 16, 2004 Section D questionnaire response, exhibit 18, and SMW Cost Verification Report at exhibit 8. Accordingly, for the final determination, we calculated a single weighted-average cost for this CONNUM. As to the Respondent's argument that the cost for this product should be excluded from the average cost calculation because sales of the product are outside the ordinary course of trade, the issue is moot because we find that sales to the stockpile were not outside the ordinary course of trade. See the Department's Position at Comment 10, above.

Comment 24: General and Administrative Expenses - Solikamsk Desulphurizer Works (SZD)

The Petitioners note that at verification, the Department found that the Respondent excluded certain non-operating income and expense items from the calculation of the G&A expense rate reported for SZD, the affiliated company that produces granular magnesium from magnesium products purchased from SMW. The Petitioners argue that all non-operating items should be included in the calculation of SZD's G&A expense rate.

Department's Position:

We agree with the Petitioners. At verification, we reviewed the details of the excluded non-operating items and noted that they related to the general operations of the company. Accordingly, for the final determination, we included all of SZD's non-operating items in the calculation of the G&A expense rate for SZD.

Recommendation

Based on our analysis of the comments received, we recommend adopting the positions described above. If these recommendations are accepted, we will publish the final results and the final weighted-average dumping margin in the Federal Register.

Agree____ Disagree____

Joseph A. Spetrini
Acting Assistant Secretary
for Import Administration

(Date)